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ROADS WITH DESTINATIONS: A CASE STUDY OF GOVERNANCE AND RURAL INFRASTRUCTURE IN NEPAL
A CASE STUDY OF GOVERNANCE AND RURAL INFRASTRUCTURE IN NEPAL
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Table of Acronyms and Exchange Rates

CDO   Chief District Officer
CIAA   Commission for Investigation of Abuse of Authority
CTO   Central Treasury Office
DDC   District Development Committee
DfID   Department for International Development of the UK Government
DSCO   District Soil Conservation Office
DTO   District Treasury Office
FfW   Food for work
GDP   Gross Domestic Product
GNP   Gross National Product
HMG   His Majesty's Government of Nepal
LDO   Local Development Officer
MLD   Ministry for Local Development
MoF   Ministry of Finance
NGO   Non-Government Organization
NPC   National Planning Commission
NR   Nepali Rupee(s)
UC   User Committee(s)
VDC   Village Development Committee

Nepali Rupee exchange rate: US$1 = NR 67.70 at 11/26/99

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I
Introduction

Grand corruption in government procurement and infrastructure projects has long been a familiar story, from bloated defense contracts to the gravy train of bridge and dam construction. At least as important, but less publicized, is the routine leakage of resources financed by the development budgets of poor countries – funds intended to build schools, establish health clinics, extend rural roads. In this context, systemic corruption erodes basic infrastructure and social safety nets, distorts the allocation of public resources, and wastes scarce funds, including international aid. Among the programs plagued by the most persistent corruption are those dealing with rural infrastructure. Whether these programs provide payment in cash, food, or some combination of the two, leakages of 30 percent or more of total project costs have been estimated in several developing and transition countries.[1] The broader costs of such corruption include reduced income to poor communities who need the resources most; creation of low-quality, high cost, and short-lived infrastructure; and encouragement of public servants and others to appropriate public resources illegally for private gain.

This case study focuses on an example of how such corruption has been addressed in Nepal. There, leakages from labor-intensive infrastructure works funded by Food-for-Work (FfW) have traditionally exceeded 50 percent.[2] The present study examines one especially effective response to this type of corruption. It asks to what extent the measures adopted in that instance provide a useful model for the governance of rural public works and other types of infrastructure projects, and it presents some lessons from this experience. Given the large number of developing countries that are aid-dependent, it is critically important to consider the role of international donors in the governance of recipient countries – and the present case study places this concern in the foreground.

The study is based on a review of relevant literature and on fieldwork carried out in October 1997 and September 1999 by a team of local and international researchers assembled by the IRIS Center, University of Maryland. It is also the result of over four years of work and observation in this area by both IRIS and its Nepalese partners. The first phase of the research (1997-8) was funded by the World Bank. In this presentation, the names of individuals have been changed or omitted to protect confidentiality. The names of key donor agencies and programs have also been disguised in order to avoid unnecessary controversy, although their identity will be obvious to many with intimate knowledge of Nepal.

This is the first of a series of case studies commissioned by the Global Democracy and

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[1] Beier et al (1993), discussions with foreign aid agencies. The same percentages have been cited elsewhere. For example, a World Bank memo made public in 1998 estimated the leakages of Bank-financed development expenditures in Indonesia at 30 percent. A former Russian Prime Minister complained that "30 percent of our humanitarian aid is invariably stolen." Marshall Goldman, "Stop Turning a Blind Eye to Russian Money Mischief," The International Herald Tribune. October 15, 1999, p.10. Earlier reviews of large FfW programs in Asia and Africa estimated leakage at one-third. Clay (1986).

[2] Beier et al op.cit. More severe losses have been possible in Nepal largely because of the significant difference between official and market wages for unskilled labor and materials. The estimate of 50 percent leakage is a conservative one, based only on losses from reduced wages paid to laborers. The mechanism of this manipulation has been illustrated, and the amount of earthwork done by a laborer in a day for different types of soil has been recorded, in relevant project documentation (see below).

Governance Center of the U.S. Agency for International Development. The overall objective of this activity is to create analytical and training materials appropriate for use by policymakers, donor representatives, and activists attempting to address systemic corruption in developing and transition countries. The case study series aims to provide useful models, lessons, and analytical tools in support of those efforts.

Summary

The study examines an effort to combat endemic corruption in the rural infrastructure programs of Nepal. This anti-corruption campaign arose *within* an international donor agency-funded development program. That initiative, the Churia program of 1993-4, used the modality of Food-for-Work to provide short-term paid employment, and to construct rural roads and other small infrastructure, in poor food-deficit areas of Nepal. The implementation team, including a group of idealistic Nepalese professionals supervised by staff of the donor agency, decided to look carefully at how existing programs of this kind were implemented and to avoid the pitfalls.

The existence of waste and corruption did not surprise them, but its pervasiveness and the size of the losses were shocking. They estimated, conservatively, that 40 to 50 percent of the resources budgeted for these programs disappeared. Several types of wrongdoing contributed to this leakage:

- Projects were awarded as political favors, not on the basis of need identification and analysis;
- Implementation was frequently handled by contractors selected in a rigged or "managed" bidding process;
- Bribes and kickbacks provided recompense for collusive project selection and contract awards;
- Manipulation of labor productivity norms and wage rates created a large extractable surplus, based on mis-reporting of compliance with standard national norms and pocketing the difference;
- Grain, cash, materials, and transport budgets were routinely misappropriated.

A complex of factors contributed to this situation. Government in Nepal has traditionally been centralized, secretive, and feudal in orientation. The country's ten-year history of electoral democracy has brought significant change to the capital, but has barely begun to address power relations in the countryside. Infrastructure programs, including those funded by Food-for-Work, have long served as vehicles for patronage and for illicit extraction by underpaid officials. The overstaffed civil service devotes a large share of its energies to ensuring that such programs provide them margins for misappropriation. Salaries pay only one-half to one-fifth of the average official's cost of living. Bureaucrats involved in public works programs are able to manipulate a system of complex and out-dated *estimation methodologies* to create margins for misappropriation. Over-estimation and over-invoicing easily create margins of 50 percent of project costs to be shared among cooperating contractors, engineers, local bureaucrats, ministry supervisors, and auditors.

Thus, corruption is both systemic and highly systematized. It is sustained by *perverse incentives, information constraints, wide discretion,* and *weak accountability*. Although the democratic change of the 1990s has brought with it attempts to strengthen constitutional watch-dog bodies and a series of *decentralization* reforms, the detailed information that could serve as the basis for a system of accountability in this area is still treated in practice as an official secret. To date, politics and administration remain substantially centralized in practice. This reinforces the chain of corruption by intensifying failures of transparency and accountability, and discouraging locally-financed and -

monitored development initiatives.

The Churia program team could not hope to break down this entire system, but they did find a way to insulate their projects from severe corruption, and in doing so to provide impetus for local reform efforts. They designed the program around the concept of enlisting local beneficiary communities ("User Groups") in efforts to design their own projects and to monitor them in such a way that losses to corruption were kept to a minimum. These communities "owned" the projects in the sense that they identified them and contributed to their design, they made counterpart contributions of 20 percent, they supplied their own labor (paid with rice and cash supplied by the program), and they assumed ownership and responsibility for the resulting infrastructural assets. This provided them strong *incentives* to police the use of project resources, since any losses came out of their bottom line.

The program's governance model enabled the User Groups effectively to act on these incentives, by maximizing *information flows* and *accountability requirements*. All information about project selection, design, standards, estimates, rates, outputs, budgets, expenditures, and participants was made fully public in project agreements, registers ("project books"), signboards, and public discussions. Using this information, the community together with the program consultants imposed accountability at regular public events, including the *public audit* at which output was measured and all payments and expenses accounted for. Regular inspections, training and orientation meetings, and other forums also stimulated information exchange and helped identify accountability issues.

What were the results of this approach? Corruption decreased and productivity increased dramatically. The momentum of this effort inspired numerous follow-on initiatives by donor agencies, government, and communities. The main results were:

- Overall, corruption declined significantly, and leakages were dramatically reduced.
- Losses of grain, the principal mode of labor payment, decreased from approximately 50 percent to about one percent.
- Productivity of the infrastructure-building work improved by roughly double, based on comparisons of costs and project completion rates with traditional programs.
- More rapid project completion enabled communities to undertake additional projects, thus increasing their benefits.
- The program's methodology enabled previously excluded populations to participate, and established patterns whereby communities held officials and others accountable for resource expenditures and results.
- The program's momentum carried over into local elections, policy changes, and follow-on programs all reflecting the Churia methodologies.

The major follow-on to Churia was the RW Program, in which two donor agencies established a similar program in partnership with the government. This program continues to date, using some of the Churia approaches to safeguard efficiency and accountability. Unfortunately, important changes that this program made to the Churia model, combined with its much larger scope and the increased role of the Nepalese government, have caused some backsliding into previous patterns of corruption. A major shift that has re-opened opportunities for corruption in the program is the use of mandatory national work norms and wage rates. In the absence of especially stringent monitoring, the policy of using national norms encourages bureaucrats once again to manipulate estimations and wage payments for personal gain.

What lessons can be drawn from this experience? The most important ones for policymakers and international aid donors appear to be these:

Make programs accountable to beneficiaries. This can be done by maximizing User Groups' involvement in design and planning, guaranteeing local autonomy in project-related decisionmaking, and providing the necessary training and support for community members to act as managers and monitors. In doing so, it is also important to balance competing interests in program governance, in order to preserve local initiative and to avoid domination by local elites or national authorities. In a sense, the ultimate aim is to strengthen beneficiary communities' entitlement to good governance, since the potential for sustained progress depends on this.

Insist on transparency of program information. This entails providing clear project standards in public documentation, and ensuring regular public monitoring and discussion. Since information alone cannot impose accountability (and may sometimes confuse the issue), it is equally important to make information public in a usable form – and then use it.

Align incentives. This is always easier said than done, especially in environments of systemic corruption. One choice that may be required in such a situation is to use the model of "cocooning" or insulating a program from corruption by setting up a parallel implementation structure. An alternative approach that could also be used as a complement is a combination of "ringfencing" (protection through detailed conditionality) and bureaucratic incentives that encourage clean administration of a program by state actors. These approaches incur significant risks of unsustainability (in the former case) and clashing incentives (in the latter). At least as important are community incentives to combat corruption, such as individual reward and overall community benefit.

Donors should act responsibly as governance institutions. Ultimately, donor agencies are part of recipient countries' domestic governance arrangements, willy-nilly. Success in this role requires sending clear signals that integrity is important, avoiding trade-offs where certain goals are achieved at the price of significant corruption, and building carefully on past program successes.

Break out of the cocoon whenever possible. Creating an enclave of probity does little in itself to address the long-term problems of governance. However, establishing patterns that survive the program and reach beyond its boundaries is a way of encouraging reform, however limited. The means of doing this include enabling communities to apply transparency mechanisms beyond the confines of their projects, cultivating political allies and emphasizing the benefits of these mechanisms to them, and finally, encouraging policymakers to adopt the program's transparency mechanisms as law.

Develop strategies to confront resistance. Programs need to identify methods in advance for dealing with the inevitable opposition by those who depend on systems of corruption. The strategies here include forging alliances to outflank the corrupt, tying officials' hands through public integrity pledges, and ensuring that program implementers themselves set an uncompromising example of probity.

The text of the case study, immediately following, begins in chapter II by describing in detail the nature of systemic corruption as it confronted the Churia program team. Chapter III then provides an analysis and diagnosis of the problem, looking at systems of corruption in Nepal and the institutional arrangements that appear to encourage them. The fourth and fifth chapters examine the strategies used by the Churia program and the follow-on RW initiative, and their impact on corruption and program efficiency. The final chapter presents the main lessons of this experience.

II
The Problem

In 1992, the Nepalese government (His Majesty's Government or HMG) and Bilateral (an international donor agency) launched a forestry project in the Churia catchment areas of eastern Nepal. This program aimed to reverse the rapid deforestation of the area caused by a combination of land fragmentation, increasing overpopulation, and lack of established sustainable forestry management systems. One project mechanism included the creation of non-forest employment options for local people.

Late that year, a severe drought struck the Churia project zone, causing dramatic declines in available work for the landless 40 percent of the area's population. In response to a request from HMG for disaster assistance, the project management hired Consult (a local consulting firm) to assess the drought situation and provide some options for relief. Their study identified the main problem as extremely low income leading to constrained access to food. Strategies to increase off-season employment would therefore have to be part of the response. Consult and the forestry project managers, with support and guidance from Bilateral officials, undertook to develop a mechanism using Food-for-Work (see Box 1 below) to support paid labor on civil infrastructure works such as roads, fishponds, irrigation schemes, and river control measures. It was also critical to use resources carefully, hence mechanisms of participatory management that safeguarded the use of money and food became paramount in the initial design.

Following this advice, in 1993 and 1994, Bilateral funded Food-for-Work programs in Siraha and Saptari, two eastern *terai* (lowland) districts of Nepal, under the aegis of the forestry project. The programs operated during the three-month period of the off-season, when labor demand is low and family income substantially reduced. This experiment was subsequently expanded into a five-year FfW project intended to reach 45 of Nepal's 75 districts. Implementation of this, the Rural Works (RW) program, began in late 1995 and continues to date.

New Program, Old System

The Churia Food-for-Work project team had an idealistic bent. It combined young Nepalese professionals, dedicated to social uplift and participatory development, with more experienced technicians. The group included former government officials who hoped to use their insiders' knowledge of development administration to effect change. The leaders were two men whose development experiences had convinced them of the need for uncompromising standards of integrity and professionalism. Ram, a director of Consult and a former HMG engineer, led the team and managed the program day-to-day. Fred, a professional staff member of Bilateral, obtained the support of his agency and its HMG counterparts for the project, and provided the team with needed advice, support, and supervision.

No sooner had the Churia program been conceived than its management team found themselves confronting a system that threatened to undermine the program from the start. Infrastructure programs in Nepal, including those funded by Food-for-Work, have long been a morass of fund diversion, misappropriation, bribery, and other forms of corruption. Though the existence of corruption did not surprise the Churia team, its extent and costs did. They estimated (conservatively) that under the

traditional FfW system, *between 40 and 50 percent of total program resources is siphoned off for personal gain by those implementing the programs.* Of these funds, approximately one-third goes to either contractors or User Committee members, and the rest is paid to politicians, civil servants, and others at various levels. These have been known to include the Local Development Officer (LDO, a representative of the central Ministry of Local Development), the District Development Council, National Food Corporation staff, rice suppliers, and others.[3]

Box 1: Food-for-Work Programs

Food aid was originally developed as an emergency measure aimed at providing immediate food relief to victims of either man-made or natural disasters. The aim is a short-term one -- to provide food for victims of a disaster until the local inhabitants can rebuild.[4] Grain is provided free of charge to NGOs and government agencies to distribute in disaster areas.

An extension of this concept is the now-familiar Food-for-Work program. Under these programs, rice, wheat, or other grain (sometimes other foodstuffs or cash) have been provided for payment to laborers in return for their work on civil construction, rehabilitation, or maintenance. This introduced a longer-term objective to a system which was traditionally short and intensive in nature. The programs largely been done on a group basis, with either contractors or NGOs/civic groups providing the labor under the supervision of government officials and occasionally donor advisors. Local politicians favor this type of program, because of extensive poverty in the villages and the lack of public sector resources at that level. The varied emphases of works programs have led to their categorization by objective, e.g.: (1) relief works, (2) long-term employment programs, (3) income-augmenting programs, and (4) low cost infrastructure programs.[5]

The use of Food-for-Work in public works programs has been a common thread in development assistance in Nepal through the last thirty years. One agency alone provided over 11 million dollars in food aid for the rural works sector from 1977-1992, when it stopped the program due to operational problems. These projects were selected and centrally executed through the Ministry of Roads and Transport. However, projects have often not been carefully chosen to provide maximum benefit. Subsequent work such as that in the Churia program has demonstrated the superior returns to ponds, irrigation canals, and other assets as compared with roads. Moreover, inattention to incentive issues in design and planning have, as in the case of India, led government implementers to use contractors to carry out the projects. This undermined the goal of local wage employment and tended to encourage corruption.[6] Some observers say it is impossible to find any infrastructure built under traditional FfW programs, since their primary objective and only reported outcome was the distribution of rice – with HMG and donors having little, if any, specific idea about who received rice and what was done in return. An important contributing factor to these problems, the fact that projects are too numerous for adequate supervisions, continues to date.

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[3] IRIS and its research partners confirmed this information through detailed interviews both in the capital and in several districts in the field, from numerous politicians and civil servants who declined to be named but admitted to the breakdown.

[4] It was also a mechanism to relieve developed nations' surplus stocks.

[5] Clay (1986).

[6] Hirway and Terhal (1995), Hossain and Akash (1993).

Among the mechanisms the Churia team found operating in Nepal's infrastructure programs are the following (these are summarized in Table 1 below):

Selection of projects. The siting of new works, particularly roads or trails that enable access to previously inaccessible areas, occurs largely on the basis of political horse-trading ("Where's my road?") rather than social or economic analysis. The prevalence of this pattern undermines the legitimacy of the public sector and tends to promote the exchange of non-transparent, including illicit, benefits. The decisions regarding which districts get rice allotments are also politically driven. National MPs want funds channeled to their electorates, regardless of local identification of needs or available resources. This is also true for resource allocation from the District Development Council (DDC, local government at district level) to the Village Development Council (local government at the village or village-cluster level).[7]

"Managed" or non-existent bidding competition. Collusive or rigged bidding is common in Nepalese practice. Payments are frequently made to potential competitors to ensure that they either do not bid, or bid in amounts higher than the bribing firm. In addition, the estimated cost of the job might illegally be made available to bidding firms for a "fee", and then all firms agree to submit bids at or above this costing level. Potential bidders, for example, may agree not to bid, and the chief engineer agrees to increase the cost estimate for the work. It is also not uncommon for contractors to face strong competition and as a result, bid the contract at less than half the estimated price. The "magic" here lies in the slackness of estimation formulas used (see below). This is particularly true in the case of earthworks, which generally constitute more than 70 percent of the total cost of an infrastructure project, though similar practices are used for estimates of materials, transport, and skilled labor. Under these conditions, contractors have no problem going as low as 40 to 50 percent of the estimated cost, carrying out the job, and satisfying the "stakeholders" with kickbacks. Margins are shared evenly through kickbacks to the engineer, the selection committee, and colluding contractors. During construction, payments are made to supervisors of works contractors to accept substandard materials, or progress which may lag behind the agreed progress schedule (including no progress at all), or structures that violate engineering quality standards.

The (theoretical) benefits of a competitive bidding system are foregone in the case of a civil works program where the works are to be implemented through User Groups (i.e. the community of prospective beneficiaries) and their representative User Committees (UCs). Such programs require the funds to be handed over to the User Committees, and the use of contractors is not allowed. Formation of User Committees is left "to the village." In practice, since there is little supervision, User Committees often consist of village-level contractors with special leverage on the local power structure, and political manipulation and corruption are probable.

Over-estimation, over-invoicing, rate arbitrage. A combination of dated estimation methodologies (see Box 2) and tight information control make it possible for project administrators to manipulate project costs and thereby reap sizeable illicit margins. Government engineers and contractors traditionally estimate a project's unskilled labor requirement and cost consistent with national work norms and wage rates – or even somewhat below this. As the project is implemented, the labor requirements and costs are reported accordingly to the responsible central ministry, but all the relevant information is kept from the beneficiary community. In the field, laborers are paid in accordance with

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[7] Public works programs everywhere have tended to become politicized. For example, the successes of the Rural Works Program in East Pakistan helped sway voters in the 1965 election. The program then became a vehicle for patronage, with consequent increases in cost and deterioration in performance. Thomas (1974)

local work norms and wage rates – or even slightly above this. Local rates are much less generous (and increasingly set on a performance basis).

Other project parameters are also subject to manipulation. The engineer might, for example, misreport the types of labor tasks involved, e.g. recording the removal of loose soil to a distance of five meters as the removal of clay or stony soil, or removal to a distance of 20 meters. "Ghost workers" may appear on the payroll. Surveys are sometimes ordered that are unnecessary or overpriced (work norms for surveys are estimated to be inflated by four times) or both. The quantity, quality, type, or brand of structural materials could also be misreported. On materials procurement, government purchasers and vendors together are thought typically to skim ten percent or so on small purchases, and about 25 percent on large ones.

The various manipulations are conservatively estimated to yield secure windfalls of 50 percent of reported project costs, which can be appropriated by the engineer, shared with other colluding parties, or used for kickback payments by contractors. The differential is neither recorded in the project accounts nor revealed to outsiders among local community members, local government, or the laborers. Auditors generally have no basis for determining whether the estimates and costs are inflated. Usually in Nepal, they only have the training and resources to check the conformity of invoices, receipts, and other documents with the project estimates and budgets. In addition, government auditors, like other Nepalese bureaucrats with oversight and approval authority, are known in some cases to solicit bribes in return for favorable reports. Reports are common of traditional FfW projects that have been carried out only on paper – i.e. where rice has been spent but no work undertaken. As one villager put it, "our landscape is littered with the bodies of unfinished projects, or projects which were paid for but never started."

Misappropriation and sale of grant inputs. Governments will either accept grant inputs from donors, or purchase them centrally and provide them as a "free" good to construction sites. Those with access to these inputs may simply appropriate them and sell them to private sector contractors. For example, a bureaucrat may take delivery of such an input (steel wires for example), look the other way when the contractor uses half the number required for the job and sells the remainder, then split the profits with the contractor.[8]

Misaccounting of cash, payoffs to accounts staff. Government accountants are known to have manipulated project accounts for gain. Payments are sometimes made to unrelated third parties and charged to contract accounts, while others are made early or in excess of agreed amounts, or with inadequate or non-existent supporting documentation. The accountants are then paid a portion of the illicit funds in return for "regularizing" or burying such records. Food-for-Work programs use cash advances to pay for transport of rice and materials, as well as for purchase of materials.[9] These payments, as well as grain storage and other costs, are routinely inflated.

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[8] A Japanese grant providing steel wires for river bank stabilization in Nepal has been terminated, apparently due to observation of this practice (although the precise reasons for this have not been made public).

[9] In the current RW program, cash for materials alone amounts to more than NR 40 million ($656,000) for twenty districts.

Box 2: Estimation Methods and Corruption

Few outsiders to the public works arena recognize the decisive impact that estimation methodologies have on the potential for corruption in infrastructure projects. The definition and periodic adjustment of pricing and engineering standards determines the range of acceptable cost and productivity levels. Where these norms contain a large amount of slack, or where they are applied to local projects in regions with vastly different labor and materials markets, they enable bureaucrats, local authorities, and contractors to create and exploit significant margins through collusion. Thus, the appropriateness and transparency of estimates is an important governance issue.

The Food-for-Work programs in Nepal provide a clear illustration of the problem. There are two main elements involved in estimations for labor-intensive civil works projects:

- the formula ("work norm") used to estimate the output of a defined unit of unskilled labor, and
- the daily or per-unit wage rate.

In Nepal, government policy generally requires the use of nationally-defined work norms, which are not only antiquated (dating from the 1960s) but widely believed to be far too loose. For example, the work norms for simple earth work (digging and removing soil) are thought to be two to three times more generous (i.e. understating worker productivity) than local practice and labor markets in most regions of Nepal. Daily wage rates are set by committees of central government engineers and other officials in the districts, and are automatically adjusted upwards by ten percent per year.

The way in which estimation methods create margins for corruption is best illustrated by a simple *example* typical of FfW projects. A five-kilometer road is to be built, with a width of four meters and the depth of earth-filling fixed at 1.5 meters for the entire length of the road. This yields the following overall figure:

Earth removal estimate = 30,000 cubic meters (i.e. 5000m [length] x 4m [width] x 1.5m [depth]).

The *standard cost calculation* for this would be something like the following:

National work norm, simple earthwork (loose soil) = 1.43 cm per unskilled labor day.
Estimated labor requirement = 21,000 unskilled labor days.
Typical district daily unskilled wage rate = NRs 100.
Total unskilled labor budget = NRs 2.1 million.

By contrast, a typical *local work norm* for this activity is 3 cm per unskilled labor day, the operative norm in many terai districts. This yields the following:

Estimated labor requirement = 10,000 unskilled labor days.

An efficient FfW project might pay *a local wage rate* of 3 kg of rice plus NRs 3 per labor day in a terai district (the rate used in the Churia program). A kilo of rice might cost NRs 10 to 15. Taking the average of NRs 12.50 would yield the following:

Total unskilled labor budget = NRs 405,000 (10,000 x ([12.50 x 3] + 3)).
Net savings = approximately NRs 1.7 million.

This means that using local labor norms and rates in this case yields an unskilled labor cost estimate of less than one-fifth of the national norm-based estimate. Even using the national work norm with the same wage rate of 3 kg of rice plus NRs 3 per labor day yields an unskilled labor budget of NRs 850,500, more than twice the requirement based on local norms, but only 40 percent of the standard cost estimate. Keeping this information hidden enables corrupt bureaucrats and contractors to engage in profitable manipulation and arbitrage.

Additional problems arise when a civil works program provides grain as the principal payment for labor, as in Food-for-Work programs. These programs require that the total estimated funds be handed over to local User Committees, and contractors are not allowed. Specific problems with FfW programs include the following:

Grain misappropriation and sellback. Payments to laborers are supposed to be provided in grain and cash. In traditional Food-for-Work programs in Nepal, the donor provides the rice, and VDCs collect the rice and distribute it to the ward. There are no true audits, no evaluations, no public records. As described above, the payment rate is often standardized, but what is actually paid to laborers is less, and User Committee members appropriate the residual and sell it, sharing the windfall with other "stakeholders". In addition, laborers are sometimes not paid their cash due, but are simply given the grain. The contractor could benefit twice from this, once from the misappropriated cash, and in some cases a second time from the grain repurchased from laborers at a low price.[10]

Watering rice/cutting quality/delivering short amounts. In planning grain deliveries and payments to laborers, donors and governments agree on the type of grain, quality standard, moisture content, and amounts to be delivered.[11] Commonly, rice is provided in advance in tranches, based on the work schedule and anticipated time to completion. There is a great deal of variability in these areas, and bribes are paid in return for taking delivery of grain that may be substandard, higher in moisture content than agreed upon, or in short amounts. Rice may be skimmed at the center, the district warehouse, or the User Committee – or some combination.[12] In some locations, already written-off rice from previous years has been supplied to clients, even when it is not edible. The rice supplied for the current year is then sold off, and the resultant funds shared among storekeepers and other collaborators.

Exaggerating rice losses at different stores. Storekeepers report losses of rice during storage. Some loss is natural due to changes in humidity and other factors. Nevertheless, it has been reported that profiteers at the User Committee level and at the district stores appropriate the rice, report it as natural "loss," then request that the authorities write off the loss. Weaknesses in public sector monitoring systems make it difficult to detect such stealing.

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[10] As laborers may need a small amount of cash for salt or oil or kerosene, they may resell the grain back to the contractor -- at a profit to the latter.

[11] A good sample of rice is provided for bidding purposes. However, once the delivery arrives, the rice quality is often much poorer. The standard tenders are called nationally, and the districts do not have the equipment or capacity to check quality in terms of moisture content or rocks inside the rice. In addition, since they do not control payments, it is harder for the districts to enforce quality. The parastatal National Food Corporation generally has warehouses locally and the capacity to measure this, although this is known to provide opportunities to solicit occasional bribes from rice suppliers.

[12] Ironically, donors commonly over-estimate the quality level desired by laborers. Deliveries of substandard grain sometimes actually provide what laborers want, while officials and contractors pocket illicit money from the resulting disparity between donor estimates and what was delivered.

Table 1: Summary of Corruption in Nepal FfW Projects

Activity	Magnitude	Winners	Losers	Causes
Politicized Project Selection	Contributes to 30-50% benefit/cost deterioration.	Pork politicians Cronies and favored districts	Honest politicians Disfavored districts	Selection at political level Planning criteria loose or not enforced
Managed Bidding	Contributes to 30-50% benefit/cost deterioration.	Dishonest contractors & officials	Users Competing contractors Treasury Public	Inadequate standards and enforcement in procurement Contractor links to politicians
Bribery and Kickbacks	Contributes to 30-50% benefit/cost deterioration.	Dishonest contractors & officials	Honest politicians Disfavored districts	Selection at political level Planning criteria loose or not enforced Weak audit systems
National-Local Labor Standard Arbitrage	Norm differential creates windfall of approx. 50-60% of national norm-based transfers.	Members of MLD, DDCs, UCs, contractors on the take	Workers Users Villages Public	Tolerance by donors Encouragement by central government Arbitrage opportunity created by national norms
Mis-Accounting of Cash	Unknown, perhaps US $0.5 to $1 million.	Members of MLD, DDCs, UCs, contractors on the take	Workers Users Villages Public Treasury	Tolerance by donors Encouragement by central government Arbitrage opportunity created by national norms
Grain Misappropriation: Short Amounts Substandard Quality Exaggerated Losses	Approximately 50% grain leakage.	Members of MLD, DDCs, UCs, contractors on the take	Workers Users Villages Public Treasury	Tolerance by donors Encouragement by central government Arbitrage opportunity created by national norms

III
Problem Analysis and Diagnosis

Attacking corruption, or at least constraining its influence on the Churia program, required an understanding of the phenomenon. Its manifestations, the mechanisms of corruption used, were known to the team in large part and became more familiar as they prepared the program for implementation. Behind this lay such questions as: What logic called forth this web of corruption and sustained it? Who benefited from keeping the system in place, and who had the strongest interest in defeating it? What specific incentives and opportunities did Nepal's governance institutions create for these corrupt practices? How might the latter be denied, at least in the context of the Churia program? The team could identify the choices available to it only when these questions were answered.

Systemic Corruption Nepalese Style

Nepal suffers from corruption that is "systemic" in two senses: it appears to pervade most of the governmental system, and modes of corruption are themselves systematized. In the latter sense, the illicit diversion and sharing of public resources, sometimes called "commissionization," works according to well-known rules. This is said to be especially true in the Departments of Roads and Irrigation. When illicit funds are received, there are standard percentages to be paid to each group up the line from the locality to the central ministry. A typical system for distribution of this "black money" is as follows:

- · ten percent to the district audit office
- · ten percent to local politicians; if not there, to local engineers and overseers
- · 25 percent to the direct overseer
- · 15 percent to the district engineer
- · 35 percent to the overseeing accountant, the department, and the ministry in equal amounts
- · five percent for entertainment costs[13].

This type of arrangement reflects the systemic (in the first sense) bargaining position of each control point in the governmental hierarchy, including the power of higher-level officials to demand bribes and commissions from lower-level officials. To begin with, many civil servants, particularly those in agencies dealing with infrastructure and procurement, are posted with the understanding that they will kick back a fixed percentage of their take from graft, often ten percent, to the ministry. If a civil servant does not perform in line with this expectation, then he or she will often be transferred. Thus, the low-level bureaucrat faces pressure to obtain bribes, kickbacks, and illicit earnings from misappropriation. Bribes and commissions are widely observed to be increasing in Nepal, in large part due to the rising cost of political campaigns. An estimated 50 to 100 seats in the current parliament were taken by force or corruption. Corruption is accepted by all political parties as necessary for survival, since parliamentary campaigns now cost NRs 10 to 20 million, and rural votes can be bought for about NRs 500 to 2,000.

As a result, demands for illicit payments stretch from top to bottom. For example, contractors, line bureaucrats, and local governments often find that they must pay commissions in order for required

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[13] This information was obtained and confirmed in field interviews with informants having first-hand knowledge. These percentages, along with the overall take from corruption, are said to shift over time – the predominant tendency being toward larger sums being demanded and taken.

funds to be released. Each district in Nepal has an Accounting and Control officer (a representative of the Ministry of Finance) who controls the quarterly allocation of the HMG development budget going to the district, and who, according to several informants, frequently extracts commissions on that basis. In this way, each position with significant control over a project – e.g. technical approval, budget review, funding allocation and release, audit – obtains and protects its share of illicit money, which is distributed from bottom to top. In one version of this, ministry personnel from all the districts put the money to be paid over to the center (usually one to two percent of the relevant budget) into a "box," to be distributed to high-level officials in the capital. Several people who have experienced this system report that it imposes a rough top-down discipline, based not on formal public sector rules but on the informal rules of patronage. Since many, probably a large majority, of bureaucrats obtain illicit earnings, they can be selectively prosecuted or pressured to conform to the informal system.

The Costs (and Benefits)

Costs: In infrastructure works, resources are wasted and structures crumble well before their time. Meanwhile, payoff requirements, over-invoicing, and the need to keep corrupt transactions secret raise the costs of these projects. Corruption thus plays a role in perpetuating macroeconomic instability, slow growth, and poverty.[14] According to a recent IMF monograph:

> ...corruption increases the number of capital projects undertaken and tends to enlarge their size and complexity. The result is that, paradoxically, some public investment can end up *reducing* a country's growth because, even though the share of public investment in gross domestic product ...may have risen, the average productivity of that investment has dropped.[15]

New capital projects are generally favored, since they provide the kinds of benefits to corrupt officials and contractors that operations and maintenance expenditures cannot. Thus high corruption is usually associated with (i) high public investment, (ii) low operation and maintenance expenditures, and (iii) poor quality infrastructure.[16] By one estimate, public works corruption has increased the cost or lowered the quality of infrastructure in some countries by 30-50 per cent.[17] The under-supply of public works and paid employment can be expected to have a ripple effect across the economy generally. Inadequacies in transportation, water, health and other types of infrastructure acts as a drag on trade and productivity.

In Nepal, systems of overestimation, over-invoicing, and commission payments drive up the costs of small infrastructure programs -- and it is widely believed (with some justification) that larger and more complex projects yield still higher corruption margins, in absolute if not percentage terms. Official estimates and expenditure figures, where these are known, make Nepalese infrastructure programs, particularly road-building projects, look more expensive than comparable activities in other Asian countries.[18] In short, Nepal, one of the poorest countries in Asia, appears to get less infrastructure at higher cost than other countries in the region. Moreover, of the approximately NRs 40 billion annual

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[14] IRIS (1996) pp. 16-23. Pope, ed. (1996) pp. 75-84.

[15] Tanzi and Davoodi (1998) p. 1.

[16] Id. p. 5-9. Wade (1982) pp. 314-17.

[17] Rose-Ackerman (1996). There is also evidence that high levels of corruption draw public resources away from education and health spending, towards large procurements of equipment and infrastructure. Mauro (1996).

[18] There is no evidence that the Nepalese public gets more for its greater expenditures. Indeed, using a conservative estimate of over-invoicing to adjust the figures for Nepal would bring them more into line with regional standards.

development budget for Nepal, approximately 75 percent goes to civil construction. The majority of this funds large projects in such sectors as roads and irrigation, the most costly of which are externally financed by loans and grants with a small government counterpart contribution. Using a conservative estimate of 25 percent leakage from civil works expenditure, this puts the cost of waste and corruption in Nepalese infrastructure programs well over U.S. $100 million per year, excluding interest on debt-financed projects and added repair costs for construction at lower than specified quality. Corruption has probably taken at least U.S. $10 million (again, a conservative estimate) from Nepal's Food-for-Work infrastructure programs over the years.

Figures such as these should be treated with caution. Corruption everywhere is difficult to quantify. In Nepal, it is doubly difficult because project estimates are treated as official secrets, and those found to have released them can face administrative sanctions. Some such information has surfaced informally, and endless examples are cited in the press. For example, HMG has recently sought external funding of NRs 450 million, against NRs 150 million in local counterpart funds, to construct the proposed 17.8 km Malekhu-Dhadingbesi road. The press published an estimate that only one quarter of this total, NRs 150 million, was actually needed to complete the work.[19] It is widely believed that construction costs in Department of Roads projects are typically at least twice as high as comparable projects carried out and monitored by communities themselves. The construction of one local road is reported to have been estimated by the Department of Roads at a cost of NRs. 700,000, but the community apparently organized to carry out the same project on a Food-for-Work basis at a cost, in rice, of less than ten percent of the official estimate.[20]

Systemic corruption also warps major government institutions. Opportunities for graft draw more participants into the corruption game, thus potentially increasing state intervention, leakages through corruption, and diminished productivity of public investment more generally. In Nepal, some bureaucratic posts are said to be "auctioned," and in any event, patronage appointments mean that competency and merit suffer. Also, the administration has little time left to attend to the public – government offices are considered a "nightmare" except for those who profit. The need for secrecy in illicit dealings means that files and decisions are closely held, and senior officials keep major approvals to themselves, processing them at home after hours so that they can discuss and negotiate them in private. Maintaining such a system also requires that the official watchdog bodies be either neutralized or coopted. Thus, the Commission for the Investigation of Abuses of Authority (CIAA) and the Auditor General are hampered by lack of capacity, and their findings frequently ignored.[21] The parliamentary Public Accounts Committee itself includes members suspected or charged with corruption.

The resulting lack of public financial discipline in Nepal is starkly evident in these official figures from 1997: off-budget expenditures equal to ten percent of the national budget, "unsettled expenditures" amounting to NRs 22 billion, and misappropriation of NRs 4.5 billion in government funds. Also, major corruption scandals come to light with alarming frequency.[22]

Winners and losers: Who wins in the Nepalese system? Civil servants and politicians are the main beneficiaries. Certain government departments have been identified as "cream departments", where

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[19] "Costliest Road Ever Approved," The Kathmandu Post, Sept 4, 1999.

[20] In another project, five years of work and NRs 5 million were reported to have been invested in road gravelling, but an investigation found no evidence that any such work had been done.

[21] Ironically, the CIAA staff suffer from the same pay shortfalls as other civil servants; worse, they are temporarily seconded from other agencies and hence subject to pressure from their home departments.

[22] UNDP (1998), Shrestha et al (1998), private discussions.

a civil servant is sure to make additional money from misappropriation and bribery. Positions in these departments are highly coveted, and transfers/appointments require illicit payments to appointing officers within the civil service. The most lucrative are reported to be the Roads, Irrigation, and Water Supply Departments, and the Ministry of Local Development – i.e. agencies with major infrastructural development responsibilities. As a result, reform proposals, such as updating work norms and instituting performance audit systems, have been resisted by government engineers and contractors.[23] Village elites (e.g. landowners and business people) also benefit from payoffs, since they usually control either local civil works contracts or User Committee operations. The benefits to officials and elites have assumed the character of an entitlement, based on a long history of undemocratic and extractive governance.

Who loses? The most clearly identifiable losers are:

(i)   villagers (including many poor populations) who lose valuable infrastructure and employment opportunities;

(ii)   districts, officials, and political representatives who do not have access to graft, or who do not participate in it, and find themselves ignored in the allocation of public works programs; and

(iii)   contractors who lose opportunities to participate in infrastructure programs due to collusion.

Given this picture, where are the pressures for reform and accountability? The general population suffering harm from corruption is relatively powerless for several reasons. First, information on the level of the corruption and the social consequences is effectively concealed. Second, until very recently (1990 and thereafter) there were no democratic mechanisms available to address corruption; even if the panchayats used extractive mechanisms, they could not be voted out. Third, those who must champion reforms are very often dependents of the existing corrupt system. Last, any attempt to deal with rent-seeking and misappropriation is likely to face problems of collective action. Overall losses to the economy translate into individual losses that, in most cases, would be counterbalanced by the costs to any individual of becoming informed and taking action to cure the problem.[24] However, because the scale of graft begins at a level immediately visible to villagers, and since corruption can easily arouse moral indignation, attempts to mobilize local anti-corruption movements are sometimes met with success. This is one of the advantages of devolving rural public works to the village and User Group level (see below).

Causes

What ultimately caused the problem? Where did the norms, mechanisms, and practice of governance fail, and create an opening for corruption? A number of systemic weaknesses undermine disciplined and efficient use of public resources, compromise the integrity of rural public works programs, and foster corruption. These are discussed below. The section immediately following places these in the broader institutional context.

Perverse incentives played an important role. Most obviously, a mass of underpaid civil servants

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[23] Nepal's system is by no means unique in this regard. A review of engineering standards used in Indonesia, for example, suggested that those were equally, if not more, lax. In Bangladesh, manipulation of work norms in FfW programs is reported to have made possible underpayment of laborers in the range of 17 to 27 percent. Hossain and Akash (1993).

[24] See Olson (1965) and (1982).

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presides over a series of planning and expenditure checkpoints that, for this very reason, tend to be ineffective or even a pretext for bribery and misappropriation. Civil service salaries and allowances appear to be significantly lower than living costs for most officials, and there is strong social pressure for engineers and other officials to take illicit "black money" (or *ghoosh*) in order to supplement inadequate pay. (See Box 3 below.) Expectations of illicit supplementary earnings between two and ten times official base salary are reported by numerous informants (including both current and former officials). Many bureaucrats are appointed with the understanding that they will earn illicit income and share it with their superiors – or face the consequences (e.g. transfer or career stagnation). Added to this is the formal uncertainty of many government appointments, which are temporary in the case of most counterpart personnel for donor-funded projects, and are subject to rotation and transfer.[25]

Box 3: Opportunities for Honesty in the Civil Service

The Nepalese civil service appears far too large and costly for the work it undertakes:

- Civil service posts: increased from 22,272 in 1961 to 100,632 in 1991.
- Ministries: increased from 22 in 1991 to 27 currently.[26]
- Cost: over half of national revenue is dedicated solely to civil service salaries and allowances.
- Estimated average work time spent on assigned tasks: 15 percent.[27]

The pay situation of Nepal's civil service makes corruption almost inevitable. A simple comparison of pay scales and costs of living is sufficient to show the pervasive incentives towards corruption, and to approximate the amount of extra income bureaucrats feel they need :

Salaries and allowances for line bureaucrats and local officials (among others) are low:
- Civil servant base salary range (all figures are monthly) = NRs 2,000 to 8,000.
- Normal base salary range, district-based government engineers = NRs 4,000 to 4,500.
- Approximate base salary on average, district-based overseers and others = NRs 3,000.
- Estimated allowance for DDC Chairs and their Deputies = NRs 3,000 to 4,000.

Civil service pay falls well short of living costs:
- Estimated monthly costs of a lifestyle suited to minor government officials = NRs 10,000 to 15,000.
  This excludes periodic extra costs of social standing, e.g. :
      travel, building a house
      daughter's wedding, estimated cost = NRs 200,000
      funeral arrangements and rituals for a family member, estimated cost NRs = 100,000.
- Estimated earning requirements of minor officials = 400% to 500% base salary.
  This excludes work-related expenses, e.g.: up-front payments and periodic commissions to superiors
  for appointment to post and receipt of salary.

Earnings of comparably qualified persons in international NGOs or private companies = NRs 20,000 and 40,000.

The likely cost of suppressing differentials through civil service reform = at least NRs 10 billion, out of an overall public sector budget of approximately 70 billion and tax revenues of about NRs 30 billion.

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[25] The Civil Service Act, strengthened in 1998, prohibits personnel transfers outside of strictly-defined time limits, as well as politically-based appointments of regular staff. These rules are routinely ignored. Shrestha (1999).

[26] Source of data through 1991: His Majesty's Government of Nepal, Report of the Administrative Reform Commission, 1992.

[27] Informal estimate by a former government engineer.

Another cause is *information constraints, or lack of transparency*. In theory, the right to information (regarding "matters of public importance") is guaranteed by Article 16 of the Constitution of Nepal. Moreover, executive and legislative acts are subject to judicial review, and there have been a few judgments requiring HMG to make information on large infrastructure projects public. Though formal implementing legislation and procedures do not exist, some categories of information – such as budget reviews, draft legislation, and parliamentary proceedings – are open to the public.

Expenditure control, audit, and investigation are fraught with delay, political influence, and the failure of enforcement. The Constitution requires the Auditor General independently to audit certain government accounts, while other audits can be ordered by legislation. The Parliamentary Accounts Committee, one of the most active bodies in the parliament, examines and raises questions about the Auditor General reports. However, reporting by government units is usually delayed, and procedures for investigating and prosecuting misuse of public resources, including complaints to the Commission for Investigation of Abuse of Authority (CIAA), are cumbersome and ineffective. CIAA investigations at district and lower levels are delegated to the Chief District Officers, who are themselves frequently a part of the problem.

In practice, information in Nepal is made available on a "need to know" basis, or for payment. The need to submit requests or complaints in writing imposes barriers on the large number of poor, rural, and often illiterate citizens who interact with the public sector. Verbal requests, meantime, carry no weight and are largely ignored. Also, beneficiaries rarely have any of the information on program budgets that bureaucrats control – and often use to their advantage. As discussed previously, the most lucrative official secret in the rural infrastructure context is the difference between national and local norms. This differential creates an arbitrage opportunity, as in the case price controls that foster local black markets: the official price of the labor is artificially high, hence administrators trade at a lower price while mis-reporting to the national level, and pocketing the difference. Somehow, the information on local markets fails to enter into national formula-setting, and improved monitoring is needed to constrain the exploitation of national-local price margins. The availability of these rents also encourages other forms of corruption, including bribery, patronage appointments, and collusion in contract bidding.

The other main causes of corruption problems addressed here can be summarized as *unconstrained discretion and weak accountability*. The systems governing public works in Nepal, though not dramatically different from elsewhere in the region, especially foster inefficiency and corruption. As a result of compromised tendering and procurement systems, only an estimated 40 to 60 percent of equipment and supply procurement (60 to 80 percent of construction services), is handled through competitive bidding.[28] Another problem is chronic lack of coordination in infrastructure planning. Resources are distributed on the basis of aggregated local and regional shopping lists, with priorities fixed according to political calculations. Transparent planning criteria do not exist in most areas, and hence cannot exert discipline on the process. Moreover, budgeting processes and know-how are rudimentary, and (at least at lower levels) result in category-wise distribution of available tax revenues rather than informed capital and operations expenditures. Weak expenditure and control systems mean that planning, budget, and procurement information cannot be used effectively, hence attempts to subvert the integrity of rural works projects usually do not face much countervailing pressure within the government.

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[28] Shrestha et al (1998).

Administrative Environment

The quality of public works governance derives in large part from institutional structures and incentives affecting the public sector. Especially where projects are located at a distance from the capital, effective governance depends critically on planning systems, on the power arrangements between central and lower-level authorities, on the flow of information to monitoring bodies, and on the nature of private or civic involvement in projects. Nepal's institutional arrangements are weak on all these points. In theory, Nepal's constitutional bodies[29] and its political checks and balances could help restrain abuses in the public works system – but these institutions cannot effectively intervene at the district and lower levels, and may themselves be compromised.

Public Finance and Decentralization: The ability to make autonomous decisions on the use of financial resources is one of the key factors in determining the level of authority vested in local government. In Nepal the DDCs have direct control over only about ten percent of the annual amount of government expenditures in a district.[30] This problem arises from a combination of disparities between responsibilities and tax assignments, the size of local tax bases, and the design and enforcement of available tax instruments. As a result, transfers from the central government and foreign aid play a dominant role. This strengthens the hand of MLD and line ministries, district representatives of the center, deputies in the national assembly who lobby to obtain a large share of resources for their constituencies, and local elites who help broker center-periphery resource flows. For these reasons, VDCs and local organizations have a relatively weak voice in planning public works and in mobilizing resources.

The structures and incentives provided by a decentralized administrative structure have an important bearing on the tendency of works programs to encourage, or undercut, self-help. FfW and rural infrastructure programs are less effective in the absence of local autonomy:

> One of the main problems [with FfW programs] was that the measures were not always in keeping with the wishes and priorities of the target groups. Thus, emphasis was placed on constructing roads in the district, whereas villagers are more interested in irrigation facilities, for example. Therefore, the target groups felt less responsible for the maintenance of infrastructures established or rehabilitated by FfW measures...The Government has learned from these experiences and, within the scope of its decentralization policy, has transferred responsibility for identifying, planning and implementing FfW measures to district and village level.[31]

Also, in Nepal, many local assets such as irrigation canals and roads were traditionally maintained by self-help practices, called *bigauti* or *hasheri* systems, required contributions from all users. Heavily centralized fiscal and transfer systems (along with foreign aid) have destabilized these traditional practices, hence villagers have come to expect government or donors to take care of local assets.[32]

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[29] These include the Auditor General, the Judiciary, and the Commission for Investigation of Abuses of Authority.

[30] Predictably, Kathmandu and other "Metropolitan" municipalities raise much larger shares of local revenue than this.

[31] Meagher et al. (1999) citing 1995 project document.

[32] HURDEC (1994), HURDEC (1996a). Studies of programs in Bangladesh have made similar findings. Hossain and Akash (1993).

Box 4: The Context of Governance

The following factors have strongly influenced the patterns of governance seen in Nepal today:

(i) The *physical structure* of Nepal has created a great degree of isolation and limited both outlook and potential growth. Its population of approximately 22 million lives in three zones along its long, narrow area. These include the flat plains area or terai to the south, the hilly regions in the center, and the high mountains of the Himalayas. Rugged terrain has created both unique pockets of tribal populations with their own languages and cultures, and some of the most isolated conditions anywhere in the world. It is not unusual for people to live days' walk from any navigable river, road, or airstrip. The road, rail, and other infrastructure is very limited, with just over 7,000 miles of road and only 52 miles of rail. Infrastructure is exceptionally costly to develop. Literacy levels are very low, at 55 percent for men and 25 percent for women, and there is a very serious shortage of skilled labor. Therefore, access to new ideas and techniques has been severely constrained, and modern concepts of business and government have been slower to emerge than in some other nations. A further complicating factor is the population's heterogeneity, Nepal having more than sixty different ethnic and caste groups, dominated by Bahuns, Chhetris, and Newars.[33]

(ii) Nepal's *economy* is chronically weak. GDP, estimated near $20 billion, is growing at about 2.8 percent per year, while the population , over 90 percent rural, is growing at over 2.3 percent per year. Recent studies indicate levels of severe poverty in almost half the population, and per-capita income is under $200. Agriculture continues to employ over 90 percent of the population, accounting for 42 percent of GDP. Industrial activity and manufacturing is very small, and mainly includes agricultural processing and handicrafts. Landlessness is common, with only five percent of the population estimated to control 40 percent of agricultural land. Unemployment is estimated at ten percent, with underemployment at 40 percent. Significantly, Nepal has been highly aid-dependent for much of its recent history. By one estimate, foreign aid accounts for some 80 percent of national development expenditure, and overall public sector budgets are usually derived approximately 40 to 45 percent from external resources, including grants and loans.[34] As a result, the incentives for reform appear to be comparatively muted and may have encouraged the deferral of reform.[35]

(iii) *History, politics, and culture* in Nepal evidence a highly stratified society. Feudal extraction of wealth from peasants by landed gentry and monarchs has been a common practice. Until 1990, Nepal was an absolute monarchy under the reign of the Shahs and the hereditary civil service family, the Ranas. The legitimacy of extractive behavior was set firmly in place early on, and it is still considered socially and politically acceptable to require very high standards of living in order to lead, no matter how the resources are acquired. The fact that the Ranas became *de facto* rulers meant that patronage in lieu of professional competence, and payments of bribes for performance of duties, became entrenched in the civil service. Unions and the civil service have become extremely politicized down to very low levels, providing allegiances to powerful senior politicians. Loyalty to *afno manche,* or "our men", becomes the mechanism for moving up. The Nepalese monarchy reinforced its powers through the traditional institution of the *Panchayat f*rom 1951 until pressure for change led to political liberalization and a new constitution in 1990, establishing a constitutional monarchy, multiparty democracy, formal separation of powers, and human rights guarantees. Executive powers are now vested in the prime minister and council of ministers. Though an independent judiciary was a stated goal of the 1990 constitution, the judicial system has suffered from political interference and corruption. The political structure is depicted in Figure 1 below.

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[33] Shrestha (1998) pp. 1-2.

[34] Id., Ranjitkar (1996) p. 11.

[35] Some scholars suggest that countries deriving over 30 percent of revenues from donors experience more severe governance problems, since they have not been forced to negotiate reforms with local mercantile classes who normally supply the bulk of public revenues. Moore (1997). Brautigam (1992).

Figure 1: Political Structure of Nepal (National Level)

Political Structure of Nepal (National Level)

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                        His Majesty the King
                                 |
                                 |------ Raj Parishad
                                 |       (State Council)
          _____
          |                      |                    |
   Executive Body         Legislative Body      Judiciary Body
     (Cabinet)              (Parliament)        (Supreme Court)
          |                 _____|_____         |
          |                 |                    |        |
          |          Rastriya Sabha      Pratinidhi Sabha |
          |          (National Assembly  (House of        |
          |           60 members)        Representatives  |
          |                               205 members)    |
   Different Ministries,                           Different Appellate Courts
   Departments, etc.                                        |
          |                                          District Courts
   Chief District Officer (CDO)
          |
   District Level Line
   Agency Offices
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Though the balance of power remains decidedly in the hands of central government and its officers, the idea that the DDCs and VDCs should play a greater role in local governance has long been on the policy agenda. Repeated efforts have been made since the 1960s to decentralize Nepal's unitary system, based on the notion of building local capacity through delegation of responsibilities under overall HMG "guidance." The Local Governance Acts of 1992[36] attempted to take these changes a step further, providing for local multiparty elections and assigning increased authority, control and responsibility for development interventions to District Development Committees (DDCs), Village Development Committees (VDCs) and municipalities.[37] In May 1999, the current parliament enacted, a new decentralization law, the Local Self Governance Act. The Act takes some further steps to devolve policy initiative and fiscal resources to the DDCs and VDCs, within the unitary structure.[38] Importantly, this law, perhaps even before its passage, had the political effect of emboldening some DDCs to develop more ambitious development plans and political agendas than they otherwise would have. However, the new law has not yet been implemented, hence the previous legislation remains the most relevant to a discussion of recent events in Nepal.

The policy of concentrating the management of development efforts at the district level or below, has been difficult to implement. The Local Development Officers (LDOs) provided by the center to the DDCs, and donor programs supporting decentralized governance, notably those of UNDP, DANIDA, and DFID, have been providing support and expertise to DDCs and VDCs to overcome their information and capability gap.[39] The government has also put forward programs aimed to foster local development management, allocating from NR 300,000 to 500,000 for each VDC.[40] However, practice has proved somewhat intractable, and the DDCs exercise more political initiative in rural development than envisioned on paper, as does the central government, consistent with its "guidance" role.[41]

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[36] The District Development Committee Act, the Village Development Committee Act, and the Town Development Act.

[37] Bienen et al. (1990).

[38] All district-level units of central ministries are to be absorbed by the DDCs, although this is expected to happen in staggered fashion across districts and no timetable for this exists yet. Critics note that the Act leaves in place the old problems of central ministries' dominance due to vague overlaps of authority (including in such areas as transport and irrigation) and the lack of fiscal resources at the district and lower levels. Panday (1999).

[39] UNDP (1995a), (1995b).

[40] This includes such programs as Self-Reliant Development, Build Our Village Ourselves, Target Group Development, the Village Development Programme, and the Rural Development Fund. *Id.*

[41] Shrestha (1998) pp. 5-6, 16-21. UNDP (1995b).

Box 5: Administrative Framework for Local Development in Nepal

The general administrative framework for local development programs in Nepal is as follows.

VDCs (Village Development Councils). The VDC– comprised of a secretary, a technical assistant and a locally elected political body-- is responsible for development activities within its jurisdiction. The secretary and the technical assistant are civil servants who are also supervised by the Local Development Officer (LDO) in the DDC, besides being supervised by the political representatives of the VDC. The VDC reports directly to the DDC and is also dependent on it for the release of the standard central government grant of Rs 500,000. Any activity or program implemented by a line agency can also be implemented by the VDC within its political borders, depending on the availability of funds. Overlapping of programs between the VDC and the line agencies is possible, and VDCs do not directly work with line agencies in most cases. The VDCs also forward their annual programs and budget to the DDC. A VDC's programs are approved by its general assembly every year, but are adjusted according to actual funding levels and timing.

DDCs (District Development Councils). The DDC is comprised of the LDO and his/her staff, and the district-level political body chosen by indirect election.[42] In principle, the DDC coordinates with all the line agencies in the district and also has its own programs and grants from the central government. The DDC reports to the Ministry of Local Development (MLD), where there is a separate division to look after local governance issues. The MLD releases the grant from the central government to the DDC. The DDC also forwards its annual program to the MLD. A general assembly of the DDC approves not only its annual programs but also that of the line agencies in the district; however, they have no control over the latter's funding or operations in practice.

HMG (Central government). All the line ministries (including the MLD) forward their annual programs to the National Planning Commission (NPC) and the Ministry of Finance for approval and budget allocation after they have been approved by the line Ministry. Depending on the availability of resources, the NPC and/or the Ministry of Finance asks the line Ministries to make necessary changes in the proposed budget and program. This process may or may not involve consultation at the local level; at times, the NPC and MoF operate unilaterally on budgetary changes. Finally, the revised budget and program are forwarded from the districts to the line ministries and then to the NPC and MoF via the regional offices, departments, divisions (within the ministries). All the approved budgets and programs are put in the "Red Book," or official national budget document, which is printed and circulated after being approved by the Parliament.

Planning: "Central" and "district" lines of program authority are vaguely defined in practice, and subject to manipulation in the planning process.[43] Districts, towns, and especially VDCs have been hard-pressed to counter pressure from the center and unable effectively to use powers given them by legislation. Planning involves two processes that parallel and ignore each other: (i) a somewhat democratic process of works planning extending from the lowest (ward) level to the district, and (ii) a second process in which line ministry representatives at the district level forward their recommendations to their superiors at the center, who in turn prioritize and forward them to the National Planning Commission (NPC) and the Ministry of Finance for final screening and decisions on budget allocations. In theory, these two processes should connect and communicate with each other, but in practice they usually do not. Line ministry personnel at the district level have been known to forward district plans to

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[42] There is a Chief District Officer (CDO) who heads the civil servants in each District; he is an independent officer under the Home Ministry.

[43] Even where a bright line has been drawn using size or cost criteria, central officials have responded by aggregating smaller into larger projects or by pushing more complex designs. Meanwhile, their local counterparts often subdivide projects to fit them under the tender thresholds.

the center *before* the DDCs have a chance to meet and provide their input.[44] As a result, not only are the grassroots preferences identified by local planners ignored, but the central government, the donor agencies, and the local governments frequently plan and implement programs in ignorance of each other's agenda. Political pressures routinely lead to the creation of too many projects, based on seemingly ad hoc "shopping lists," with too little funding. Bureaucrats usually approve the majority of requested civil works projects, but with small amounts of funding. As a result, half-built roads and bridges collapse during the rainy season, and may cost several times the standard budget to build over a period of years rather than all at once. Even if they had the will to control all public works projects, neither the DDCs nor the central oversight agencies are capable of tracking the vast number of projects in existence.[45]   This creates overlap and other failures of coordination that waste resources and encourage misappropriation.[46] An example of the system for public sector fund flows and control is depicted in Figure 3 below.

Several responses to this have been put forward. The World Bank has put HMG on notice that future loans will depend on performance, and the leading bilateral donors have formed a coordinating committee on governance and expressed their concern to the government. There have been abortive attempts to institute participatory district planning methods as well as sectoral master plans. Where government has turned to "participatory" project development and implementation models, these have often resulted in departments forming Users Committees at their own initiative, keeping them in the dark about project plans and resources, and using them as rubber-stamps.

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[44] Meagher et al (1999) citing Panday 1999.

[45] Some districts have 50 or more projects ongoing at a given time. By one informal estimate, there are more than 15,000 incomplete projects in the water supply sector alone.

[46] An example of this is the situation where two entities have budgets for the same or overlapping projects – e.g. the Department of Roads and some combination of MLD, the DDC, and a donor agency each targeting construction on the same stretch of road – with the result that the work is completed and the extra budget resources misappropriated.

Ministry of Local Development

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                        ┌─────────────────┐
                        │ Cabinet Minister│
                        └─────────────────┘
                        ┌─────────────────┐
                        │    Secretary    │
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┌──────────────┐  ┌──────────────────────────┐  ┌──────────────────┐  ┌─────────────────────────┐
│ Line Divisions│  │Special Development Bodies│  │ Line Departments │  │Local Infrastructure Project│
└──────────────┘  └──────────────────────────┘  └──────────────────┘  └─────────────────────────┘

┌────────────────────────────┐   ┌────────────────────────────┐        ┌──────────────────┐
│General Administration Division│ │Technical Engineering Division│       │  Regional Offices │
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│Policy, Planning & Program Division│ │Women Development Division│       │  District Offices │
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│ Local Governance Division│
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│Municipality│ │   Rural    │ │  Training  │ │Decentralization│ │    Vital     │
│ Management  │ │Development │ │ Management │ │  & Legal     │ │ Registration │
│            │ │            │ │            │ │ Consultation │ │              │
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┌──────────────────────┐
│District Development  │
│     Committee        │
└──────────────────────┘

┌──────────────────────┐
│Village Development   │
│     Committee        │
└──────────────────────┘
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Source: MLD

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Figure 3: System for Public Sector Fund Flows and Control

System for Public Sector Fund Flows and Control*

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┌─────────────────────────────────────────────────┐
│   Budget speech & grant for scheme approved (MoF) │
└─────────────────────────────────────────────────┘
                         │
                         ▼
        ┌──────────────────────────────────────┐
        │   Funds entered into "Red Book" (MoF)  │
        └──────────────────────────────────────┘
                         │
                         ▼
     ┌─────────────────────────────────────────────┐
     │      MoF authorizes MLD to use funds          │
     │  and sends CTO letter that MLD is authorized  │
     └─────────────────────────────────────────────┘
          │                              │
          │                              ▼
          │              ┌───────────────────────────────────┐
          │              │  MLD informs CTO about internal    │
          │              │ allocation of budget, and informs  │
          │              │ and authorizes DDC to spend budget │
          │              └───────────────────────────────────┘
          │                              │
          ▼                              ▼
  ┌──────────────────┐      ┌───────────────────────────────┐
  │ CTO informs DTO  │◄─────│  DDC requests DTO release first │
  │that budget approved│     │ installment of funds to DDC and │
  └──────────────────┘      │              VDC                │
          │                 └───────────────────────────────┘
          ▼                              │
  ┌──────────────────┐                   │
  │ DTO releases funds│◄─────────────────┘
  │to DDC/VDC account │
  └──────────────────┘
          │
          ▼
  ┌──────────────────────────────────┐
  │ DDC/VDC releases first installment │
  │   to UC after procedures completed │
  └──────────────────────────────────┘
          │
          ▼
  ┌──────────────────────────────────────────┐
  │ For each further installment, UC provides  │
  │ VDC with details of previous installment   │
  │ expenditure, progress report, and expenditure│
  │ plan for the current installment.          │
  └──────────────────────────────────────────┘
          │
          ▼
  ┌──────────────────────────────────────┐
  │ VDC provides DDC with details of first │
  │ installment expenditure, etc. and requests│
  │ next installment                       │
  └──────────────────────────────────────┘
          │
          ▼
  ┌──────────────────────────────────┐
  │   DDC releases next installments   │
  └──────────────────────────────────┘
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*Rural Development and Self-Reliance funding

MoF: Ministry of Finance
CTO: Central Treasury Office
MLD: Ministry of Local Development
DTO: District Treasury Office
DDC: District Development Committees
VDC: Village Development Committees
UC: Users Committee

IV
Squeezing Corruption Out of the Program

The Churia team's efforts to establish an effective program faced a system where nearly half of the resources disappeared due to the varieties of theft, collusion, and abuse practiced by those in positions of responsibility. Most who knew about these losses considered them an unavoidable cost of doing the business of project implementation. In any event, existing systems of administration, public finance, civil service employment, and government oversight helped entrench systems of corruption. However, the Churia team decided they could not simply resign themselves to the misappropriation of a large portion of program resources. The costs to the program and to the communities that needed it were simply too great. This meant they had to find a way to ensure that program resources reached the beneficiaries, and doing this required something other than business as usual. They had to keep systemic corruption out of the program. And, they had to do so from their position outside the government, with only the carrots and sticks of donor agency influence and public opinion to back them up.

But how? Wholesale public sector reform could hardly be imagined in any but the longest-term scenarios – absent a severe crisis. On the other hand, implementing the program through the usual government channels would essentially halve the resources going to needy communities, and send a further signal that foreign aid funds were fair game for misuse. Ignoring the government altogether posed the risk of non-cooperation, even obstruction, and demanded a free-standing structure – a difficult prosepect. Then again, a compromise that made the support and cooperation of government available would likely mean the sacrifice of some portion of resources, if not entirely through corruption, then partly through incentive payments to ensure that civil servants would play along. Any realistic option, other than business as usual, depended critically on two sources of counterpressure against official efforts to misuse program resources: first, the aid agency, Bilateral, along with its Nepalese contractors and collaborators, and second, the beneficiary communities themselves with their political representatives. Could the program mobilize support from these two sources? Depending on that level of support, where should the program situate itself along the spectrum from complete independence to total reliance on government as the implementing agency?

The Churia team focused on changing three central elements of the governance system for these projects. First, *accountability* had to be given a local nexus. Since the administrative systems of the central government could not be relied upon to maintain integrity, the main program stakeholders – users, communities, and their local political representatives – had to play the primary watchdog roles. To align incentives most effectively, the design needed to foster a sense of community "ownership" over the program. It did so by requiring a local match or contribution to all projects, and by devolving to the communities authority over the management of project resources and the maintenance of the infrastructure created.

Second, the *incentives* of the key implementing personnel had to be radically revised. This required the fullest possible delegation of program management to an independent parallel structure – the management team set up by Bilateral and its Nepalese partners to implement the project. In the Churia team's view, only in this way could the project escape most of the dysfunctional culture of government in Nepal, particularly the pressures towards corruption experienced by civil servants. An independent structure enabled the team to control pay, performance review, and other aspects of the implementers' framework of incentives. Still, government involvement in aspects of policy, planning, and logistics could not be avoided.

Third, *information channels* had to be opened in both directions, between program management and the beneficiary communities. This meant both providing communities a strong voice in the program and imposing strict transparency requirements with respect to all project decisions. This approach, virtually unprecedented at the time, confronted severe restrictions on information flows between policymakers and administrators, on the one hand, and beneficiary communities on the other hand. Not only did the public have little input into program design and implementation, but government felt virtually no obligation to provide data on public finances and program administration to the public. Monitoring, quality control, and accountability were largely a matter internal to the administration, and the establishment of formally independent watchdog bodies did not change this situation perceptibly. With its monopoly of information, resources, and authority, government felt little pressure to restrain bureaucratic discretion or to provide communities a forum for signaling their priorities and preferences.

Transparency of program information was handled in the most straightforward way: all proposals, designs, estimates, plans, uses of materials, purchases, wage payments, labor rolls, and project management decisions were made public both verbally and in writing, and project records were to be accessible at all times. This encouraged communities and their political representatives to monitor the activities of all those involved in the program, and to hold them accountable if anything went awry. Although this began only as an arrangement between the international donor-provided project staff and the communities themselves, central and district-level bureaucrats as well as local politicians soon found their discretion restricted.

These changes are presented in more detail below. The story of these program governance reforms began in 1993-4, but evolved over a six-year history of relief program implementation, redesign, and resistance. The Churia team's efforts to carry out a foreign aid project soon took on the guise of a campaign for administrative, political, and cultural change. In this campaign, the team could usually count on the support of communities and their political representatives, because the latter had come to understand that good program governance meant substantially increased benefits for them.

The Churia Program

Bilateral accepted the recommendations of Consult's initial report, to provide a timely Food-for-Work program through simple, locally managed systems, supporting the construction of local civil works, particularly ponds, irrigation canals, riverbank protection, and rural roads involving a high proportion of earthworks. The Churia program hired Consult to design and implement the relief scheme (with key input from Fred, of the Bilateral staff). Success in the first season convinced the managers to try this system a second time in 1994, to see if it would reduce the numbers of poor Nepalis who cut trees for income during the slow agricultural periods. The project zone was expanded from a single district (Saptari) to include a neighboring district (Siraha). Also, the previous program was reviewed and some corrections made. The program provided all construction materials, all skilled labor, and performance-based wages of one rupee plus one kilo of rice per agreed local measure of earthworks, plus a small amount of cash for inputs such as pipes. Experiments were also conducted, of requiring local contributions for the projects of 20 percent in the form of materials or labor.

Over its two years, the program evolved a set of implementation procedures emphasizing participatory management and transparency. Cost estimates were prepared by Consult using local costs and labor norms adjusted for tasks of varying difficulty. The VDC Chairmen and Secretaries took

responsibility for implementation, work organization, record keeping, rice storage, and distribution through representative User Committees. The DDC was responsible for policy formulation, VDC selection and overall monitoring and dispute resolution. A set of guidelines for program implementation was written and widely distributed. Each project kept a project book for public consultation, containing the essential features and costs of the program, detailed maps of each project, along with measurements, input and cost estimates, and changes.   All information was conveyed in simple Nepali language. Orientation sessions were held on the working principles of the programs, the process, and the role of stakeholders for VDC and DDC staff as well as users – before project selection. The public audit process, in which records of works progress and payments would be physically verified in the presence of the User Groups, was discussed in each area in a series of open meetings with laborers and other villagers, and it became a firm pre-condition of disbursement of future tranches. Lastly, the reward for those completing their projects was priority consideration for follow-on projects.

Inevitably, there were some difficulties in implementing this system, but it succeeded.   The results were startling. Overall cost-benefit estimates for the two project periods include:

- total management costs of 12 percent
- rates of return on investment of over 42 percent per year
- unit costs of less than 50 percent of traditional estimates[47]
- a 90 percent completion rate
- rice loss rates of less than one percent.

These numbers can be compared with worldwide Food-for-Work results showing achievement of less than 30 percent of the target activities, food losses of 30 to 50 percent, and substantial cost overruns.[48] Only ten percent of Churia projects were terminated due to local inertia or loss of rice tranches, and projects were carried out at less than half the usual cost. The program operated at several times the usual pace and completion rate for traditional civil works programs in Nepal. In 1993 alone, the target was to complete up to one project in 114 VDCs and one municipality, and supply work to 7,000 persons. In fact, over the ten weeks of field activity, the project supported 180 projects in 108 VDCs that were independently certified as complete. Over 80,000 poor persons benefitted from over 370,000 work-days paid during the program. The results in 1994 were even better: the program covered 118 VDCs (out of 120 initially planned), and implemented 300 village level projects.

The Churia Governance Model

A new model of project governance emerged from the Churia experience, with these features:

Local determination and "ownership" of projects. In the VDCs where the project operated, an orientation training followed visits by the project professionals. Each VDC then had to determine the available labor force in its area, and hold a mass meeting to choose a list of potential projects in the area based on needs and demands of their constituencies. Of the original 120 VDCs, 118 did so, focusing largely on regeneration of dilapidated ponds, irrigation canals, riverbanks, and roads. Following this,

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[47] HURDEC (1994).

[48] Beier et al (1993) pp. 5-6.

program consultants worked with each VDC to identify users[49] and facilitate the establishment of a User Committee vested with responsibility for achievement of project goals. However, the village as a whole was expected to watch over the projects, and user meetings often were attended by the entire village. The laborers came first from the User Group, then the surrounding village, then the VDC, and finally from adjoining areas if the labor pool was not sufficiently large locally.[50] The consultants, VDC staff, and villagers jointly assessed cost and labor requirements, and prioritized requests in terms of feasibility, land availability, and benefits to users. While the DDC made the ultimate determination regarding the projects, the establishment of selection standards and independent enforcement of these standards by Bilateral and consultants (and later by the VDCs themselves) ensured selection by developmental criteria rather than patronage.

Four elements of the local determination process proved essential to its success. First, prioritizing and selection of projects took place at local public meetings, discussions included all salient details, and agreements were signed in public. Second, the works were selected (at least partly) based on the ability of the local community to participate, which meant using local labor for earthworks and other tasks, rather than using more complicated or mechanized options. Third, the project staff ensured that the local people had virtually all the necessary tools and knowledge to complete these projects themselves, ensuring a high level of ownership and pride.

Finally, the two governing committees were fundamental in project operations. User Committees were made up of trusted individuals selected by village public meetings. This group managed physical implementation of the project, organizing laborers, and measuring earthworks progress. For example, in one village, the local people selected two laborers, two women, two farmers, and two businessmen to be members of their User Committee and to represent diverse local interests. Rice Control Committees were to be made up of representatives from opposing political groups, keeping an eye on each other and managing rice stocks and payments.[51] These two committees gave project control a local nexus, ensured relative political neutrality, kept information flows open to the public, and entrusted resources to people at the local level, giving them the opportunity to prove their capacity to achieve results locally. By far the majority lived up to this challenge.

Establishment of local labor norms and rates. Central government policy in Nepal sets labor productivity norms and daily wage rates on a national basis. The work norms used in estimations for various types of labor in infrastructure projects were established over 30 years ago and are estimated to be one-half to one-third of average labor productivity in this type of work. Similarly, official daily wage rates are much higher than actual rates paid to laborers locally, again as much as two to three times as high. As discussed above (see Box 2), these differentials have encouraged a great deal of embezzlement.

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[49] I.e. the community expected to reap long-term benefits from the public works. User Groups ranged from 200 to 2,000, depending on the type of project.

[50] It is important to distinguish between a user and a worker. A user in the context of Food-for-Work has been defined as the person/family who gets long-term benefit from the asset/infrastructure created through FfW. A worker, on the other hand gets only a short-term benefit in the form of wages (rice and cash). In the hill/mountain districts, users are also workers in many cases, whereas in the terai, most of the workers are not users, as they do not have access to assets in the form of land. A User Group consists of all the users benefiting from the infrastructure created/rehabilitated in the long run via increased production, houses protected from rivers and land slides, etc. In the case of roads, it is difficult to identify the users, as they are widely scattered and are highly heterogeneous in terms of interests and socio-economic conditions.

[51] In practice, the Rice Control Committees played a much less important role than the UCs, and indeed were mere formalities or even non-existent in many cases.

Box 6: The Logic of Participation in Project Governance

Local development programs generally fit into the following modes of governance:

(i) "Partnership" (or *coproduction*) in which donor and government organizations, as well as communities, bring resources, ideas, and initiatives to the table, and jointly plan the program. This approach, typical of "social investment fund" programs, maximizes local "ownership" and integrity by putting most decisions in users' hands.

(ii) "Conditionality," in which communities receive inputs in return for conditions defined elsewhere (i.e. government or donors).

(iii) "Bargaining," in which communities or local development "brokers" exploit leverage created by overriding government or donor interest in completing projects or spending project budgets. In some cases, this is the end-state of projects that have outlived a useful life span.[52] Here, principal-agent problems (misaligned incentives, information asymmetries) become most severe, with the attendant inefficiencies and misuses of project resources.

The first of these, coproduction, is a decentralized or "polycentric"[53] approach that includes several possible models for supplying public infrastructure, e.g. government provision, public works contracts, public-private partnerships, private provision, and communal provision. If appropriately chosen and structured, coproduction projects can achieve exceptional levels of efficiency, integrity, and sustainability due to the public-private synergies created. At the core of successful coproduction is a credible mutual commitment to project goals by the public sector and the community, ideally a contract between the official and civic organizations involved. Its benefits potentially include greater efficiency, more specific tailoring of works projects to revealed preferences, and decreased opportunities for shirking and corruption by public servants. The design of these projects can strengthen governance by subjecting public sector partners to transparency and accountability requirements, while the fact that the community is providing – by design – a part of the inputs limits the amount of public capital potentially expropriable through corruption.[54]

Coproduction, as in the case of the Churia and RW programs in Nepal, locates primary management responsibility in User Committees. Such committees vary in scope and effectiveness, depending on the type of asset being produced – a pure public good, or something with more 'private' characteristics. Projects dealing with roads or trails often have UCs for the limited purpose and time period of construction only, since local collective action to construct, repair, or especially to maintain a road is difficult. The cost to the individual of expending labor on it, when the alternative of 'free-riding' exists, is much greater than the average benefit of the road to the individual. Moreover, there are few means to impose the costs of a road on all users, or to exclude those who do not contribute (apart from toll roads, which are not feasible in such settings as rural Nepal). By contrast, committees in charge of irrigation and fish pond projects have tended to continue after construction is completed, in order to deal with issues of use, maintenance, and governance of the facility.[55] These works can be either 'rival' (simultaneous use by all those interested is not possible) or 'excludable' (benefits can be selectively denied). The benefits of these infrastructure works usually far outweigh labor costs for individual users. Hence, the rationale for a defined group of users to organize construction, maintenance, and governance becomes clearer.

The Churia program eliminated this graft opportunity by establishing local work norms and wage rates tailored to each district. After a brief failed experiment with daily wage rates, a piece-rate system was set up at between 10 and 25 percent above the prevailing local wage rates (i.e. local piece-rates), following lengthy discussions with laborers and local User Committees. This performance-based system

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[52] Beier et al. (1993).

[53] Ostrom (1996).

[54] Id., Isham and Kahkonen (1998). A caveat: this analysis is not meant to suggest that decentralization automatically improves program governance. It will tend to do so where beneficiary interests are effectively represented in program management – otherwise, it will tend to reinforce domination by local elites. Clay (1986).

[55] Meagher et al (1999) citing Pandey and Upadhayay (1997) pp. 9-10.

measures all tasks, e.g. the amount of earth removed and the distance of the movement, and pays accordingly. Such systems already exist locally, and are used by landowners for informal labor.[56] Work norms and wage rates were established with DDC approval, publicized widely in mass meetings, and reinforced by project consultants in regular discussions with villagers. These local labor norms and rates ("local norms") became the basis for estimating costs of projects, instead of the officially prescribed "national norms." Due to this radical approach, it was possible to generate two to three times the normal physical work output with the same financial and/or grain resources.[57]

Public information and public audit. An integral part of this program was the public declaration of information on the project, enabling villagers to be their own monitors. First, a *project agreement* between the resource-contributing agency (in this case, Bilateral) and the VDC, clearly stating the expectations on all sides, was reviewed and signed publicly. Second, A *project book* was kept with the VDC secretary or the UC secretary, and made available to anyone on demand. It included:

- a short description of the activity and works;
- estimation methods and engineering standards used;
- rates for all categories of labor to be used;
- a detailed budget, including a list of materials purchased;
- a list of the User and Rice Control Committee members as well as the full set of users;
- a list of those who worked as laborers and their payments in rice and cash;
- a "comments" section on progress and certification of measurements and rice payments by project consultants and User Committee members; and
- minutes of public meetings where progress was reported.

Completed project books dating back to 1993 and 1994 were commonly found available during the field visits in late 1997, and villagers were quite proud to show them. At the end of each tranche of work, the project book was read; measurements were made and discussed; payments were made, recorded and read; and discussion of any issues or problems encouraged. Third, bi-weekly *inspection visits* were made by donor representatives (or consultants) to check progress, ascertain successes and problems, and agree with the implementers on corrective actions to be taken before the next visit. Last, results were confirmed through *public audits*, in which all records, payments, and physical works progress were thoroughly reviewed for consistency in a public meeting before the next major phase of a project could proceed. These meetings were open to anyone who wished to attend, along with laborers, the project staff, and the User and Rice Committees.[58]

Rice payments in tranches, monitored by committees with membership from all major political parties. Project staff set up storage in the districts and subdistricts for rice distribution to VDCs, and arranged for tests of rice quality and weight. Work was divided into sections, and rice allocations made in

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[56] The standard mechanism developed to determine local norms for new projects was to ascertain local wages paid in a variety of VDCs in recent seasons, determine the highest of these rates, and pay about ten percent above that rate. This was then used as the standard throughout the district. Since labor migration between VDCs within a district is quite easy and information travels fast by discussions on the road and in markets and tea stalls, inter-VDC labor rates tend to be quite close in value.

[57] Initially, laborers themselves sometimes demanded very high wages, up to three times the norms, unless they understood that the alternative was not to have the project proceed. This suggests that prior experience with donor-funded projects taught villagers that project staff tend to place higher priority on fund expenditure than on fairness and integrity in project management.

[58] Beier et al. (1993) pp. 24, 45. HURDEC (1994).

advance for each section, with between two and four tranches provided per project, depending on the history of the VDC and User Group. Rice was moved by bullock carts hired from villagers in rotation, so that people could easily see how much was coming. A member of the Rice Control Committee kept the rice locally under lock and key. Rice payments were made in public before the User and Rice Control Committee members, and often in the presence of project consultants. Payments were accounted for in full during public audits. If all rice could not be accounted for, the next tranche was not paid. In case of overpayment to workers, laborers made up the difference in volunteer labor. If there were underpayments, the VDC or UC head was shamed publicly in an audit meeting and made to pay back the shortfall. Usually, villagers worked hard to receive their rice, and projects were completed quickly.

Implementation authority fully delegated to an external agency. Although both politicians and civil service officers were involved in the program, the actual cash and rice were under Consult's control, and the consultants had full authority over design and estimation approval, purchase of materials, and overall monitoring. This helped reduce the scope for corruption, and enabled the project to be responsive to problems as they emerged in the field. Consult became a timely and reliable presence, helping the VDCs to do the work properly and emphasizing integrity.

Where there were problems in the 1993/94 Churia FfW Program, they largely consisted of attempts to perpetuate the usual corrupt practices. In a few locations, laborers were underpaid, usually because they did not participate in the public audit. The thefts were discovered and the VDC chairmen fined by the Chief District Officers. In other locations, the User Committees or VDCs became inactive, and the projects could not proceed. In some cases of misappropriation of rice by User Committees, VDCs, or storekeepers, they repaid under public pressure. Where they did not, projects did not proceed. Word spread that successful project completion led to new projects, that cheaters did not prosper, and neither did their villages. The total amount of rice embezzled in 1993, for example, was less than ten tons out of over 2,700 tons, affecting 11 out of 118 projects. Virtually all missing rice or its equivalent was recovered.

Neutralizing Resistance

In contrast to traditional FfW programs, Churia tried to constrain incentives and opportunities for corruption by cutting through the information asymmetry between project managers, on the one hand, and communities and political authorities on the other hand. By moving maximum responsibility and initiative to the User Group and VDC level, the Churia design aimed to reduce discretionary control over project resources in the hands of organizations or individuals not accountable to the community (nor effectively supervised by the central government). The use of local labor norms substantially reduced the potential "rents" available through misappropriation. Finally, public audits meant minimal reliance on administrative audit conducted by civil servants and maximum transparency at the local level.

Clearly, this approach collides directly with established systems of corruption. It aims to take beneficial opportunities away from many of that system's traditional "winners," a relatively discrete and powerful bloc, and to empower a relatively weak and diffuse group of "losers," rural communities, to maximize returns to themselves through cooperation and vigilance. In the case of engineers and overseers assigned specifically to the Churia program, increasing transparency directly threatens their livelihood. Isn't this destined to fail? The old winners are bound to resist and to claw back the benefits to which they feel entitled. The losers will lose again because collusion, intimidation, and information control make cooperation costly and difficult. How can such resistance be overcome, or at least its effects neutralized?

Building alliances: The Churia team did it utmost to outflank the old guard through their control of important resources and their alliances with communities, NGOs, and politicians at the grassroots. Most importantly, the program's transparency mechanisms helped provide the communities, User Groups, and laborers with information about their entitlements to project procedures and resources, hence the ability to defend them. This was easiest with respect to labor payments. When public audits revealed misappropriation of rice or cash by engineers, overseers, User Committee members, or others, the crowds' anger was at times difficult to control. Some offenders were physically assaulted, while others were subjected to shouting and complaints directed to the DDC. In other cases, government counterpart resources were misappropriated, with the result that projects having community support and input could not bring the anticipated benefits – such as irrigation water reaching the fields of User Group members.

The usual outcome of such revelations was restitution of the stolen resources and a public apology. There do not appear to have been criminal proceedings against any officials, although some DDCs have used party alliances and other forms of influence with MLD to have officials transferred or temporarily suspended. More recently, the Maoist insurgency in several districts of Nepal has helped keep pressure on local politicians and HMG bureaucrats in those districts to refrain from corruption. This pressure takes various forms, including anonymous threats of physical violence against corrupt officials.

Where possible, the Churia team supplemented its community partnerships by cultivating alliances with local politicians (in the VDCs and DDCs) or alternatively with central government representatives (e.g. the LDOs), and by exploiting the conflicts between levels of the governmental hierarchy. So, for example, in the four eastern terai districts in which the Churia governance model was developed and maintained under the expanded Rural Works program (see below), the project team lobbied the DDCs and secured enactment of policies requiring the use of locally-determined work norms and wage rates. In doing so, the team had to overcome resistance by central bureaucrats in the districts, including some attempts to persuade DDC members to oppose or overturn the new policy by means of bribes and favors. In some cases, such as the Western district of Kanchanpur, this counterpressure was successful in reversing existing DDC policy on local norms. In other cases, elections changed the political balance, and the Churia team had to struggle in order to get the policy reaffirmed. In public discussions, the opponents of local norm policies made a variety of arguments, suggesting that diverging from central government norms would be illegal, that this would complicate government audits, and that norms resulting in lower pay for workers were exploitative.

Successes in this area were made possible in part because of the composition of the DDCs and their lack of access to HMG funds in the period from 1993 until 1995. District council members are chosen from among elected members of the VDCs. In 1993, there were several newly-elected United Marxist-Leninist (UML) party representatives sitting on DDCs. Like many district politicians at the time (including some members of the majority Nepali Congress Party), these representatives were idealistic, they took a reformist line, and they campaigned actively against corruption. It is widely acknowledged that this attitude has changed across the board in recent years. Also, it was not until 1995 that new central transfers such as the Village Self-Reliance Fund, and increases in financial support to the DDCs, made significant resources available for local politicians to use – and abuse.

In a few cases, the Churia and RW teams managed to win the support of central ministry representatives at the district level, against local politicians or other HMG bureaucrats. In 1994-5, the Churia project managers in the eastern terai worked with the Forestry Ministry instead of MLD as their central government counterpart. That ministry had previously adopted a national policy of using locally-determined labor norms and rates, and its support helped the project team hold the line against pressure from other quarters. In rare instances, CDOs or LDOs, who appear to be part of the corruption system in

many cases, have proven valuable allies against district-based engineers, User Committee members and others who attempted to engage in abuses.

Improving incentives: The Churia team also tried to address the severe distortion of bureaucratic incentives that encouraged corruption. Inevitably, the issue of supplementary payments to counterpart officials arose. Other programs used them – a multilateral aid project, for example, was providing supplements of 45 percent of officials' base pay, in addition to convening workshops in Kathmandu (thus enabling the officials to skimp and pocket unspent travel and per diem funds). Bilateral, MLD, and some DDCs tried similar experiments, but then abandoned them. Experience elsewhere suggests that supplements risk distorting bureaucratic incentives, fostering competition for projects (and the accompanying allowances), and encouraging the neglect of the basic, non-project, responsibilities of government. In Nepal, the supplements have always been too small to make more than a marginal difference,[59] and they usually failed to deter officials from exploiting graft opportunities. On the other hand, the Churia design already constrained graft opportunities through the use of local norms and strong transparency mechanisms. This left officials with few choices. Liquidating savings, shirking, moonlighting, seeking transfers to other districts or programs, and taking leave to work as a donor agency consultant are always theoretical possibilities. However, the usual responses in fact were complaining and attempting to corrupt the program. In at least one case, a district engineer asked a Churia project manager outright to look the other way while the engineer stole from the government's counterpart contribution.

Oddly, resistance to change came not only from bureaucrats, contractors, and politicians accustomed to illicit earnings, but sometimes also from those whom the program intended to benefit. This happened because the new approach upset expectations and created initial uncertainty. In some cases, DDC members were inclined to support the Churia model, but did not believe it could work. When traditional corruption margins and the ways in which the new system would reduce them were explained, and especially when initial experiments yielded dramatically higher productivity from program investments, the skeptics became active supporters. In other cases, people simply had difficulty imagining and adjusting their expectations to a new system where projects were not run for commissions and resources were not routinely stolen. They had no experience of such programs, and they had to be convinced before they would actively support or participate in them. For example, some local vendors of construction materials were reluctant to adjust their invoices downward, reflecting the Churia team's unprecedented refusal to accept the usual ten percent kickback. The vendors were afraid this would appear to their bosses and the outside world as though they were no longer willing to pay for official cooperation.

Setting the right tone: The Churia team was determined to break the culture of passivity, secrecy, and reciprocity that sustained the system of corruption in this particular area. The team placed its headquarters in a hotel, where members lived and held project meetings and strategy sessions that habitually stretched their working day to 18 hours during the project season. The leaders decided to send a clear signal from the start, setting a policy of zero tolerance for any behavior affecting them or coming to their attention that smacked of corruption. This included the directive that team members were not to take food and drink, even the occasional cup of tea, with officials, politicians, or others who might seek to

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[59] I.e., if the overall top-up benefit amounts to some 50 percent of base salary, that leaves the official short of her/his requirements by a minimum of 150 percent of base salary (and probably much more). Moreover, formal incentive payments are now discouraged by both bilateral donor agency rules and by policy guidelines from the Auditor General's Office of Nepal. This reduces the choices in this area to disguised incentives, such as travel and training opportunities, that are too expensive and episodic to influence bureaucratic behavior in the aggregate.

influence them with respect to the project. In Nepal, as in many countries, this is clearly antisocial, but the team leaders believed it was necessary in order to set firm and unquestioned expectations of integrity in the project. Their uncompromising standards, their zeal and abstemiousness, may have alienated some potential cooperators, but did create a general impression that the team was determined to run the program cleanly and would resolutely oppose attempts to bring the usual corrupt practices into it.

The team also made it clear that it expected no less of officials and politicians who had dealings with the project. Especially in the early stages of this process, meetings with such figures were held in groups, preferably in the presence of community and User Group members. In this way, the Churia team would engage the group in a discussion of the need for integrity in program governance, and extract public commitments from all those present to support the necessary policies and to take the necessary steps. As in the "island of integrity" concept, this approach threatened embarrassment to anyone who opposed or suggested a watering-down of anticorruption standards. It also helped set standards, provide a framework for cooperation, create social motivation to impose sanctions on anyone who deviated from the agreed norms and policies, and isolate opponents.

Where opponents of the Churia approach to program governance could not reverse undesirable policy decisions or covertly reintroduce traditional systems of corruption, they sometimes targeted members of the team. Accusations of unfairness, incompetence, and corruption were sometimes used, as well as threats of dismissal or punishment. For example, in 1993, notables from one terai village became angry that their request to have a program located there was turned down. They threatened to have members of the Churia team dismissed, then filed a corruption complaint with the CDO, attaching pages of local signatures. Ram explained the situation to the CDO and showed him that the program was in full compliance with project selection criteria, whereupon the CDO had the complaint withdrawn.

Impact

The Churia framework for civil works governance had a number of identifiable results (these are summarized in Table 2 below):

Reduced Corruption. It is difficult to measure the full decrease in corruption-related losses. This arises in part from the general problem that reliable numbers on most forms of corruption are simply not available, and in part from the fact that all elements of the reform package were not consistently in force across all project areas. However, data from Siraha and Saptari document a more than fifty-fold drop in rice leakages under the Churia project in 1993-4 as compared to traditional FfW programs. Available information on overall costs also supports field observations that bribery, misappropriation, and related program distortions were substantially reduced, at least in the 1993 and 1994 project years.   In later years, the replication of some of these governance improvements across 20 districts has no doubt made the use of resources under the RW program significantly more transparent and efficient than in comparable HMG programs. However, this benefit would likely have been much greater had more of the original governance framework been kept in place during the follow-on project (see below).

Increased Accountability.   The Churia governance design introduced greater downward accountability. This enabled local governments, committees representing the users, and NGOs acting as advisors and overseers to enforce program integrity at the local level – thus adding several dimensions of local accountability, and contributing to the decline in waste, misappropriation, and bribery. It also limited the effect of the overall patterns of upward accountability to national bureaucrats, politicians, and

cronies with respect to the programs supported by Churia. Given the nature of Nepal's political system and its mechanisms for public expenditure control at the national level, this upward accountability appears largely ineffective and itself produces distortions.

Reduction in costs and increased returns. According to the data compiled by Churia and compared to the respective DDC records on previous civil works, the cost per project under the Churia model was less than half of that in comparable traditional projects.[60] This admittedly crude comparison is nevertheless suggestive, and is consistent with information on comparisons of national and local norms for earthworks labor payments, which form up to 95 percent of the costs of rural infrastructure projects. Field engineers also reported that the recorded costs of traditional DDC projects are approximately twice the total real expenditure. This supports the general estimate of 50 percent losses under traditional programs, and confirms that the overall cost of the Churia program compared to standard civil works is much lower. Finally, although cost-benefit analyses for traditional FfW projects in Nepal were unavailable, the cost-benefit under Churia showed a repayment on investment in two years, a very high rate of return by most standards.[61]

Increase in the number of completed projects. Due to the improvements in local project ownership and outside support, the number of completed projects was very high in areas covered by the Churia model, above 90 percent of those commenced. Field engineers reported less than 50 percent completion on standard civil works projects under other funding sources due to both corruption and inadequate budgeting and delivery of resources to the field.

Increase in numbers of subsequent local projects. In each case, the villages worked hard to secure a follow-on project in their areas. The first year targets for Churia, indicative of prior experience in government works programs, involved completing one project in each VDC. By the end of the second year, most VDCs were completing two projects during the short period of off-season activity.

Increase in participation of women. From a small margin of total labor, involvement of women increased to about 30 percent in Siraha, Saptari, Udayapur, and Dhanusha (the latter two districts were added later – see below), with women holding around 16 percent of User Committee positions. This is due to efforts of the project to set up women-only projects, and to ensure the participation of women as laborers and on committees in all projects. In the project zone, this is a major change. As suggested by a growing body of research, women use incremental increases in resources to benefit the entire family more often than men, particularly in the areas of nutrition, health, and education. Women are also considered locally to be more trustworthy. Consequently, increased women's participation can reasonably be expected to improve the effectiveness and heighten the overall impact of resources provided in the project areas.[62]

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[60] Churia estimates for 1994 showed a total cost of Rs 45 million for 482 completed projects, or a cost per project of Rs 93,000.

[61] HURDEC (1994) pp. 5-6.

[62] As the final report of the Churia program stated:

The women-only projects have boosted the morale of the women, developed their confidence in managing their own affairs and opened up some new possibilities for the upliftment of poor women in the VDCs despite the restrictive traditional setting. In the context of Siraha and Saptari (which are considered to be among the very traditional and conservative societies in Nepal), these women-only programs were the first of their kind. They have generated considerable social impact among the local people. In some cases, even the relatively well-to-do women worked in the ponds (Bastipur and Fulkahakatti VDCs in Siraha). [HURDEC (1994) p. 27]. See Azfar et al. (1999).

Election of local leaders to public office. Local elections in 1997 found a number of User Committee members running for office for the first time. They felt they had acquired enough leadership skills to run for office. Many of them were elected to local or even DDC offices. When villagers were asked about this, they advised that these elected individuals had shown they could be trusted to bring resources into the village and manage them properly.

Broader influence: There have been other spinoffs from Churia in the sphere of international donor agency practice. The World Bank incorporated the findings of an earlier report on these experiences into its Nepal country strategy. Specifically, the Bank has included the transparency mechanisms developed under Churia, notably public audits, in a proposed "Learning and Innovation" loan for a pilot project in rural infrastructure that may lead to a $50 million program across most districts of Nepal. Importantly, this project will use district-level work norms, national NGOs as monitors of public audits, and other forms of verification.[63] Similar approaches have been proposed or are in use in programs supported by the Asian Development Bank and the Netherlands, among others. Some discrete elements of the Churia approach, such as wage payments in public, have been used in the past, but the current trend represents a more comprehensive and serious move towards the incorporation of anti-corruption mechanisms in program design.

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[63] Helvetas (1998).

Table 2: Responses to Nepal FfW Corruption and Results

Activity	Responses	Results	Lessons
Politicized Project Selection	Increase local voice and management for small works.	Scope for cronyism slightly reduced.	Elected officials use political criteria. Key is to make this transparent and bribery-free.
Managed Bidding	Public audits External verification Simple projects Civil servant salary top-ups and performance incentives.	Quantity and quality of works improved, and costs decreased by 50% under Churia. Evidence of less corruption	Need to reduce contractor influence on public works decisions, constrain bribery, and ensure competition.
Bribery and Kickbacks	Public audits External verification Simple projects Civil servant salary top-ups and performance incentives.	Quantity and quality of works. Improved, and costs decreased by 50% under Churia. Evidence of less corruption	Decentralized monitoring and enforcement can align incentives to increase effectiveness.
National-Local Labor Standard Arbitrage	Use local norms Public audits	Some districts implemented and thereby reduced costs and leakages. Some did not	Elites and bureaucrats will fight to maintain opportunities for corruption. Need to co-opt them through incentives and political pressure.
Mis-Accounting of Cash	User Group ownership Public audits Clean audit condition for next tranche. Civil servant salary top-ups and performance incentives.	Small reductions, but cash management still problematic.	No cash counterpart until audit systems improved?

Grain Misappropriation
  Short Amounts
  Substandard Quality
  Exaggerated Losses
	User Group ownership
	Public audits
	Clean audit condition for next tranche.
	Civil servant salary top-ups and performance incentives.
		Food leakages down from approx. 50% to under 1% under Churia.	Need to sustain combination of restricted corruption opportunities, incentives, information flow, and controls.
			If one or more of these lost, corruption can return.

V
Extending the Program

A successful experiment over a limited timeframe in two districts is one thing, a clean and effective long-term program across a majority of Nepal's 75 districts something else. How could the Churia program, with its successful governance structure, be adapted to a much larger program across a diversity of terrain and social systems? Could such a program become a means of improving governance in public works and social safety-net programs? Should greater responsibility be shifted from the donor agency to the government, and if so, should this change be sudden or gradual?

In the event, it was decided that a more ambitious program required a partnership with the agencies of government and the multilateral donor who traditionally implemented Food-for-Work programs. These institutions brought with them the political authority, as well as the administrative and logistical capability, needed to carry out a large-scale program across dispersed areas of the country. Here again, though, questions of governance arrangements arose. These included such matters as the relative contributions of each party, the framework for their cooperation, and especially the scope of Bilateral's control over such issues as site selection, fund disbursement, and monitoring procedures. (See Box 7 for a discussion of governance issues in donor-financed programs.)

In this context, it becomes evident that, whether they recognize it or not, international donor agencies working with recipient country governments (or with NGOs) frequently make project design and resource allocation decisions that have significant effects on governance in those countries. (See Box 7 below.) Hence, the configuration of what became the single largest poverty alleviation program in Nepal involved Bilateral in a set of critically important governance decisions.

Expansion under Donor-Government Partnership

How did the Churia experiment evolve into a large-scale undertaking? The successes achieved in the program during 1993 and 1994 did not go unnoticed, particularly by Multilateral (a second international aid agency). Multilateral had been operating Food-for-Work programs previously but had experienced numerous problems with them, including large grain losses and frequent failure to complete projects. After a detailed evaluation of the Churia program and discussions among Bilateral, Multilateral, and the Ministry of Local Development the Rural Works (RW) program emerged in late 1995 under a trilateral agreement between these parties.

The program aims, over five years, to mobilize approximately 15 million workdays of seasonal employment for unskilled rural workers in 45 of Nepal's 75 districts.[64] The program budget for the first three years, including inputs from HMG and the two donor agencies, was U.S. $17 million, which made it the single most important poverty-alleviation program in Nepal.[65] Over the full five years, Multilateral is furnishing some 45,000 tons of rice, 420 tons oil, funds for transport grain, as well as for materials ($280,000) and training ($220,000). Bilateral is providing advisors, vehicles and office equipment for MLD, as well as contracts with local organizations to provide project consulting services. It also

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[64] Meagher et al. (1999) citing 1995 project document.
[65] Id. citing program evaluation by Boergel et al. (1997).

monitors overall food distribution, labor use, and works completion.[66] Overall percentage contributions to the program are:

- Multilateral: 48 percent (rice and cash for unskilled labor, tools and equipment, training),
- Bilateral: 21 percent (consultants, training, tools and equipment),
- HMG: 23 percent (cash for skilled labor, construction materials, and technicians), and
- Local government: eight percent (DDCs five and VDCs three percent – cash for unskilled labor).[67]

The program documentation details the responsibilities of each participating institution. MLD selects which districts can participate. Areas are to be selected on the basis of food deficits in the hills, and high concentrations of landless laborers in the terai. The DDC and its staff are responsible for working with the VDCs to establish User Committees and select projects. The DDC staff also provide the project cost estimates and designs. (The project document does not state whether cost estimates and labor rates are required to be made public.) The DDCs are expected to fund 20 percent of the labor costs as their contribution. Official national work norms are to be used, unless otherwise agreed by all parties at the district level.[68] Projects are to be monitored by overseers and engineers provided by MLD to the districts for this purpose, with support from Bilateral consultants. Public audits are required. The RW administrative structure is depicted in Figure 4 below.)

The project started in ten western districts, with approximately one quarter of the VDCs in each district participating. New districts were added later, and as of this writing the project operates in 20 districts. The Churia program districts of Siraha and Saptari were not included in the first year of the RW program, but were subsequently brought in by special agreement, along with adjoining districts.   From 1995 to 1998, 900 projects were reported as completed, as compared with 100 incomplete.[69]

Replication Issues

The results of the program's expansion and adjustment are mixed. Field visits in the eastern terai during the second year of operations, along with reviews of monitoring reports for the first ten districts, showed significant divergence from the project document and also from the Churia program on which it was modeled.[70] This variance, particularly in governance practices, has two possible explanations. First, from a bureaucratic point of view, when a donor-funded project in two or three of Nepal's 75 districts severely constrained the diversion of project resources to theft and kickbacks, that was a relatively minor matter. With the prospect of many more districts (potentially 45 of them) using this new system to prevent diversion of project resources to district and national level civil servants, opposition would naturally stiffen.

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[66] Id. citing Boergel et al. (1997).
[67] Id. citing 1998 project document.
[68] Meagher et al. citing 1998 program document.
[69] Id. citing 1998 project document.
[70] Follow-up field research, recently completed, is consistent with these findings.

Box 7: Governance in International Donor-Funded Projects

The nature of the international donor-recipient country nexus can have important governance outcomes. First, history and international aid experiences suggest that aid dependency may intensify governance problems by further attenuating the link between a government's performance and its ability to raise public finance.[71] Second, aid programs set up a complex series of principal-agent relationships in which donors, recipient governments, and their agents and contractors have potentially conflicting interests. This creates individual incentives to negotiate arrangements at odds with the objectives of the original program agreement, as well as the wishes of the ultimate political authorities on either side – for better or worse.[72] The combination of aid dependency with conflicting objectives can undercut a recipient government's "ownership" of a program, hence its commitment to ensure success. In most poor and aid-dependent countries systems of public budgeting, planning, and expenditure are only loosely connected to agreed policy priorities – hence the phenomenon of "donor-driven" budgets and programs.[73]

Further complicating this picture is the fact that aid is *fungible*. According to the World Bank," The safest assumption for donors is that they are, more or less, financing whatever the government chooses to do."[74] In other words, aid (even in project form) usually has the same effect as general budget support. It could increase total investment in the chosen sector up to the full amount of the aid or even more, or alternatively it might simply free up resources to be reprogrammed elsewhere, resulting in little or no net increase, or even a decrease. Purely in terms of resource allocation, foreign aid is generally less effective than domestic fiscal transfers, which have a larger "flypaper effect" (i.e. "sticking" or resulting in net increases in targeted or general public expenditure in the recipient jurisdiction). Fungibility could mean that equivalent resources, instead of being invested in the donor-financed program, are allocated to "white elephant" projects, consumption expenditure, state enterprises, crony loans, and other areas prone to waste and corruption. Or, if the aid program is meant to be "additional," i.e. used in an area where the government will not allocate its own resources, the short-term impact is likely to be eroded because of the government's lack of interest and commitment. Lastly, fungible domestic resources might in fact be used productively, to match aid resources, provide complementary inputs, or finance other necessities.[75]

A number of responses to these problems have been tried in environments of weak governance. One is to design programs and conditionalities so as to protect aid resources from the worst effects of local governance problems. This could take the form of "cocooning," i.e. setting up separate structures to oversee programs independently of the bureaucracy, or "ringfencing," i.e. including in aid conditionalities stringent and detailed governance mechanisms aimed at forcing government to exempt the donor-financed program from the usual practices of waste and corruption. While these strategies may discourage misappropriation of the aid resources themselves, they do not directly address fungibility. Nor do they help in the building of necessary public sector management and governance capabilities. A second approach amounts to a kind of aid paradigm shift: foreign aid should be viewed not as a *resource transfer* but as cooperative *knowledge creation* that increases relevant forms of information and capability.[76] This, in effect, acknowledges that undesirable forms of fungibility, as well as waste and corruption, cannot be tackled in the near term, but that they may eventually be overcome by longer-term institutional development. A third approach, which has the benefit of both increasing the effectiveness of projects and limiting the potential damage caused by incapable or venal bureaucracies, is to make intensive *participation* a part of the design and implementation processes (see Box 6). Thus, all aid programs entail tradeoffs among short-term program efficiency and impact, public sector reform and institution-building, and development of local implementation and monitoring capacity in the community. Where programs simply make an "end-run" around the government, they clearly fail to address the need to improve public sector governance. In dysfunctional administrative settings such as Nepal's, the choices available pending large-scale reform might have to include selecting the country out of the aid portfolio as well as the use of parallel structures and participatory approaches.

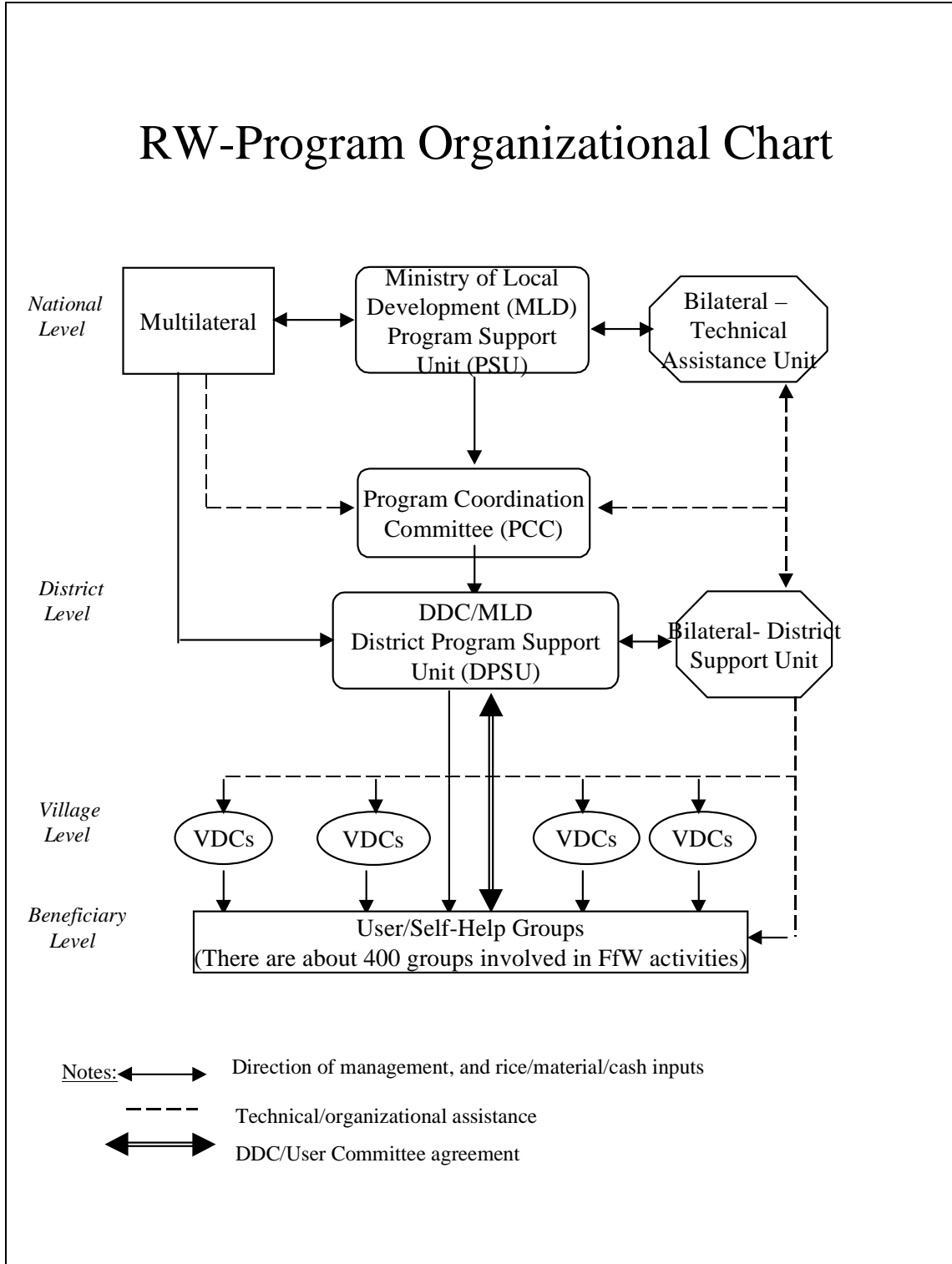
[71] Moore (1997).
[72] Murrell (1999).
[73] World Bank (1998).
[74] Id., p. 74.
[75] Id.
[76] Id.

Figure 4: RW- Program Organizational Chart

RW-Program Organizational Chart

National Level

Multilateral

Ministry of Local Development (MLD) Program Support Unit (PSU)

Bilateral – Technical Assistance Unit

Program Coordination Committee (PCC)

District Level

DDC/MLD District Program Support Unit (DPSU)

Bilateral- District Support Unit

Village Level

VDCs   VDCs   VDCs   VDCs

Beneficiary Level

User/Self-Help Groups
(There are about 400 groups involved in FfW activities)

Notes: ⟷ Direction of management, and rice/material/cash inputs

- - - - → Technical/organizational assistance

⟹ DDC/User Committee agreement

Source: Program Document

Second, in designing the RW replication, the donors appear to have paid insufficient attention to ensuring that all of the essential elements creating success in the original model were followed. Some of the changes introduced in RW are said to have been justified by the need for full partnership by the government. However, implementation through the same system encouraging corrupt practices in the past is much less likely to slow corruption. Consultants specifically told Bilateral that use of local norms and other aspects of the Churia governance model was essential for a successful follow-on project. This advice appears not to have been taken into account in implementation.

The major design and implementation issues in the RW program are these:

Political factors play an increasingly important role in the selection of districts and VDCs, with very little countervailing power in the hands of consultants and project personnel, and hence less adherence to technical criteria.[77] One DDC has openly adopted the policy of giving each of its 101 VDCs a turn at having a project. DDC members chose several projects based on overtly political criteria (e.g. siting projects in their home villages), while in others they decided in favor of projects either without assessment by the LDO or in contradiction to existing analyses and plans. As a result, some of the affected VDCs found themselves dictated to or overruled, and in some cases refused to provide their required cash contributions.[78] Bilateral consultants and staff acknowledge some of these difficulties. However, they point out that pockets of food insecurity and landless laborers exist throughout most of Nepal, that identifying needy districts and villages is therefore not a simple either-or process of choice, and that some political intrusion is inevitable in a program involving a full partnership with government.

User Committee processes sometimes undermine local accountability. While the User Groups were meant to be the initiators and implementers of projects under VDC management, the program's processes have tended at times to undercut this:

> It has been observed that formation of most of the users' committees (UC) have become a formality. UCs are not adequately aware of their roles, responsibilities, and rights. In many cases they have been "used" by non-users of the projects as rubber stamps.[79]

User Committee members in some districts view themselves as having little to gain from membership in the committees. They are often either dictated to by the DDCs, ignored, or manipulated.[80] One program report acknowledged that half of UC members are appointed by the DDCs and VDCs, most often in road and river embankment projects (where benefits are most diffuse). Usually only two to three UC members are active.[81] These failures contradict the logic of coproduction and tend to undermine project performance. The problems with Users Committees have intensified with the RW replication, but actually date back to the beginning of the Churia project.

A policy of using traditional uniform national work norms, except where local norms are specified by agreement, appears to have re-opened the window for graft. Since the use of local work

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[77] A comparison of selected districts and sites with the latest available data in 1997 showed that some were not food deficit areas, while a number of food deficit districts were not included in those selected for RW.

[78] HURDEC (1997b) pp. 7-8.

[79] HURDEC (1995).

[80] Meagher et al. (1999) citing ODC (1997).

[81] Id. citing 1998 program report. Ironically, RW has been criticized for its dependency on more or less permanent UCs and project consultants, which is thought to hinder sustainability and to ignore the need to strengthen government institutions: "the weak government structures were more or less neglected and by-passed." Meagher et al. (1999) citing Boergel et al. (1997).

norms has not been encouraged and indeed has been resisted in areas where it has been suggested, national norms have predominantly been used. As a result, incentives and sometimes opportunities for skimming have returned. Government officers in some locations not using local norms were candid in admitting they had gone back to the usual system in order to obtain reasonable "compensation." In parts of the western and far-west regions, User Committees listed part of the difference between local wages and the national norms as their user contribution.[82] Government officials from the center and district have generally not been interested in making changes (or even actively opposed).[83] One major difficulty for advisors under the RW program structure is to institute local norms under conditions where they are unable to enforce the rules by withholding rice or money. In many districts, civil servants (backed by MLD and some Multilateral officials) have campaigned vigorously against local norms. For example, program consultants went to Surkhet, Banke, Kailali, and Kanchanpur districts, spending several months on planning and implementation. Serious conflicts erupted between officials and consultants over the local norms issue. At least two of the MLD engineers are reported to have approached the respective DDC Presidents with the offer of bribes if they opposed the use of local norms.

In certain districts, the local norms were accepted and applied. These included the original Churia areas of Siraha and Saptari, along with the adjoining districts of Dhanusha and Udayapur. Some of these have adopted locally-determined work norms and rates for all projects financed by DDCs and VDCs, and intend to apply the same policy to central ministry programs being devolved to the districts under the Local Self-Governance Act of 1999. In these areas, public audits and project books have been properly kept. A few other districts have tried to use district-level norms that are not as generous as the national norms, and in a number of them, consultants and NGOs have worked hard to ensure the proper maintenance of project books. Some of these efforts have met with success, while others have not, due to a combination of political pressure and limited training and support.

Effective monitoring of project procedures and targets has become more difficult, due to the implementation of large numbers of projects in each program district, coupled with insufficient resources and authority by project consultants to address procedural breakdowns and wrongdoing. Although rate boards showing the quantity of work and wage rates are routinely used, this does not always prevent the manipulation of wage payments, especially in the absence of consultant supervision. There was evidence early on in the program of a lack of open public selection of independent User Committees in some areas. In some areas, books were blank or not available to the public, and public audits were either not held or held with small groups of interested persons, the laborers and users being largely absent. One program report estimated that project books were adequately kept for two-thirds of projects, and that 45 percent of projects actually used public audits.[84] Consulting firms and NGOs working as advisors to the project cited several reasons why public audits were not possible, e.g. the program units in the DDCs did not cooperate, the village level power structure was too strong to accept such a radical approach, and the consultants were not able to get sufficient back-up from the Kathmandu program office when they confronted problems in the field. Even in cases where public audits were conducted, the program did not require them as a precondition for release of rice tranches.

Control of construction materials acquisition, rice transport, and some other project elements by government has left those areas open to inefficiency, manipulation, and leakage. For example, National Food Corporation officials, charged with certifying the quality of rice, are reported sometimes to give

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[82] Id. citing program assessment by Pandey and Upadhayay (1997).
[83] Upadhyaya and Beier (1997).
[84] Meagher et al. (1999) citing 1998 program report.

approval for substandard rice samples in return for bribes.[85] Rice leakages in the ten percent range are still reported, especially on larger projects. Monopoly control of rice supply in some cases intensifies these problems – by one estimate, rice supply contracts for nearly half of all RW districts were held by a single supplier. In addition, rice transport is widely acknowledged as vulnerable to corruption. For example, reports from one district indicate over-invoicing of transport costs by 900 percent. Project staff and consultants report that standard patterns of Nepalese public sector management usually apply to the HMG components of the program. By contrast, the distribution of rice under the RW program is thought to be quite transparent, benefiting from a tacit "hands off" policy that exempts it from the more common Nepalese system of skimming. A bigger monitoring problem plagues the cash contributions – where bureaucratic flexibility to manipulate rice payments has been taken away, the cash component offers a readier source of illicit supplementary income.[86] In many areas, those with selection power will choose projects with higher proportions of cash expenditures, because the latter are harder to audit publicly.

The partnership arrangement under RW has thus made the maintenance of overall program integrity more difficult. In most cases, this arrangement has enabled bureaucrats to misappropriate parts of the HMG counterpart contribution, and to threaten non-cooperation or worse if project consultants tried to get in the way. In these instances, the project has had to tolerate some misuse of government resources, while policing the protected zone of donor and community inputs as carefully as possible. In some cases, bureaucrats may in fact be exploiting counterpart resources more intensively in order to make up for their shortfalls in illicit earnings. Those resources amount to some 31 percent of the total program budget. If this has indeed been happening, then the RW program may have contributed to a perpetuation, perhaps a deterioration, in public sector corruption outside the donor program enclave – i.e. requiring the government to hire more temporary counterpart bureaucrats, who exploit the resources under their control more intensively than otherwise, since the donor-funded portion of the program is off-limits. By contrast, in a few instances where the project management team had built up the necessary alliances and expectations, the partnership with HMG and local government provided a rationale to apply strict transparency standards beyond the aid-financed portion of the project, to other areas and other projects.

Pay and incentive problems persist. Officials involved in the RW program are paid a fraction of what is considered to be an adequate living wage (see Box 3). There are also reports that the motivation of some of these program administrators has been undercut by pay differentials. On the one hand, the MLD program engineers and overseers are in a weak position compared with other officials, in large part because the temporary nature of their jobs exposes them to insecurity and lack of influence.   On the other hand, consultants are usually paid significantly more than all of the officials involved. This has led to perceptions of unfairness, which may have encouraged both under-performance and corruption.[87] Experiments with salary supplements or top-ups have been tried under the Churia and RW programs. The efforts under Churia appear to have met with more success, although this may have been more a result of overall program design than of the incentive payments themselves. Currently, program bureaucrats do not receive top-ups or additional allowances for project activities (e.g. travel) that add to their existing workload and costs. Thus, there is little or no incentive for them to put any time, energy, or money into this activity.

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[85] This was confirmed by reports from the districts in late 1997.

[86] Meagher et al. (1999) citing Schulthes (1997).

[87] Meagher et al. (1999) citing Schulthes (1997). A recent study suggests that corruption derives more from bureaucratic perceptions of unfairness with respect to the reward structures than the absolute differential between public and private sector salaries alone. Van Rijckeghem and Weder (1997).

VI
Lessons

What lessons do these experiences embody? In the infrastructure programs analyzed here, it is clear that advances and retreats on the issues of audit, work norms, local responsibility, and other areas played a major role in determining the level of corruption, hence the extent of program benefits to rural populations. This highlights the need for careful design and consideration of institutional arrangements applicable to development initiatives, by both donor and recipient governments. In particular, the following points seem to emerge as the most important lessons of the experiences just reviewed in Nepal. The program design elements emphasized below should not be viewed as substitutes for formal administrative reform. Rather, they can serve as complements where such reforms are in place and effectively implemented, or as coping mechanisms – perhaps even as stimuli toward reform – in environments where they are not.

1. *Make programs accountable to beneficiaries.*

While "stakeholder participation" has long played a role in development programming and rhetoric, the Nepal experience suggests both that User Group responsibility can be difficult to establish in reality, and that the incentives such an arrangement provides for effective monitoring make it worth the effort. Administrative and political *decentralization* is a critical long-term need in this area, and one that can be facilitated in practice by the use of program-specific local accountability mechanisms. Establishing accountability to beneficiaries in these circumstances involves the following dimensions.

Maximize user involvement in design and planning: Public works programs contribute to the economy generally, but particularly with rural infrastructure, most benefits are heavily concentrated in localities nearest the sites. This is especially true of ponds, river embankments, and irrigation works. Where User Groups and communities have a leading role in designing, implementing, and monitoring programs, several important advantages arise as a result. Local preferences can be most closely matched, thus maximizing allocative efficiency and reducing waste. Informational asymmetries that create opportunities for abuse and corruption in the circuit of principal-agent-client relationships can be minimized or even eliminated. Last, incentives can be aligned optimally, since those most concerned with outputs and benefits – the users and communities – also have a robust role in design, implementation, and monitoring. The informational and incentive aspects of governance will be explored in more detail below.

For the reasons just cited, the Churia program emphasized local management and "ownership" of projects. Users (those expected to reap long-term benefits from works) were vested with responsibility for identifying and achieving project goals, and assisted in developing the necessary capacities and processes for doing so openly and effectively. The program recognized early that the effectiveness of local voice and understanding is directly related to levels of corruption. Where decision-making is further away, things can be hidden. When projects are technically complex, less of the benefits accrue locally, and there are fewer people who can understand how the project should work. Concentrating on locally selected projects helped increase interest in having them work. User Groups have an "encompassing" interest in the performance of these projects, since inefficiency and corruption tangibly reduce the benefits to the group and to individual members. Problems arising in the follow-on RW program provide an important caveat to this. If User Committees are appointed from outside, or merely used as tools or window-dressing, they lose credibility and undermine local accountability.

Guarantee local autonomy in decisionmaking: Local accountability also implies the authority to set rules, or at least to adjust standards to local realities. Where this became most critical in the Nepal case was in the area of work norms and wage rates. Locally-determined norms allowed program resources to stretch farther, and harmonized project budget figures with a clear and familiar local entitlement – thus ensuring that corruption would directly affect the workers' bottom line and elicit protests. Absent local norm and rate-setting, there is a substantial opportunity for corruption in the local-national differentials. The approach of local norm-setting was successful in the Churia program districts because it was also an absolute prerequisite for project activity. Its rationale was frequently discussed with all concerned. Politicians recognized that the benefits this brought to their areas, and the credit they earned from supporting it (or at least not opposing it), would outweigh the returns from graft that they would have received under the traditional system. In departing from this precedent, RW gave up an important check on the potential for corruption and made effective project governance more difficult.

Advise, train, and support user-monitors: Rural projects involving the poor, of course, present unique challenges, especially if these populations are to impose accountability. In situations where many are illiterate and there is a long history of exploitation, more energy and time needs to be spent explaining the systems, repeating the explanations, and ensuring that everyone understands measurements and timing. All involved parties – users, workers, officials, consultants – need to concur on project roles and approach, resource levels, accountability mechanisms, and the choice of implementing agency. It may also be important to ensure proper support from local government by training relevant personnel, both elected officials and civil servants, on roles and responsibilities.

Balance competing interests in project management and monitoring: It would be both naïve and incorrect to suggest that local accountability supplies complete assurance of program integrity, or that it should be untrammeled. Local constituencies operate with limited capabilities and information, and are vulnerable to domination by traditional elites such as large landowners and high-caste families. However, when Churia villagers set up User Committees that balanced the powers of social groups, this increased the probability that the members would prevent each other from cheating. Particular attention to the representation of women and poorer is important here. It indeed appears that those areas in Nepal where local accountability was appropriately reinforced and balanced reaped the most benefits from the programs.

The same applies to the users' interaction with outside agencies. Thus, a carefully crafted balance of power between users, donors, and government can be crucial to program success, as it was in the case of Churia. If the donors in that case granted too much power to government to dictate terms, the users suffered and corruption was reinforced. If the users did not obtain enough information or understanding, then they could not implement projects and complete them properly as "owners." By contrast, if User Groups had too much control, they tended to come under the domination of local elites, who exploited the majority more thoroughly than civil servants. Also deserving mention is the mutual discipline that intergovernmental relations can make possible within a decentralized system, for instance where allies in central ministries share an interest in program integrity and effectiveness.

Strengthen beneficiaries' entitlement to good governance: This may be the most important lesson of the Nepal experience. Critics rightly point out that implementing rural infrastructure projects mainly through a parallel non-governmental structure is both expensive and unsustainable. However, where the bureaucracy is severely compromised, this may be the only way to reverse community expectations, to build a sense of entitlement to transparency and integrity in such programs, and to stimulate formal administrative reform. There is some evidence that the Churia program, and perhaps some of the RW

projects, have achieved this. Unfortunately, whatever impetus there was toward serious structural reform in Nepal has largely been dissipated to date. Of course, this is not the end of the story, and continued efforts along this line may yet yield fruit.

2. *Insist on transparency of program information.*

This may be the most straightforward, even obvious, implication from the Nepal case (as well as the anti-corruption literature). Corruption grows in environments of secrecy, where rules and resource allocations are unclear. In the present case, this is most dramatically illustrated by the secrecy and manipulation that surrounded the use of official *estimation methodologies*. The Churia/RW requirement that all project information (including estimates) be published, and that key activities be conducted publicly, was crucial to the integrity of the programs. This made it possible for beneficiaries to monitor and defend their entitlements.   The following elements are especially important.

Provide clear standards in public documentation: Not only should all measurable elements of a project be clearly stated in order to provide standards for accountability, but this information must be fully accessible to the public. The Churia governance approach insisted on this. First, a useful foundation for project integrity is a written agreement between the resource-providing agency and the community carrying out the project. In addition to making the community explicitly responsible for managing resources and achieving project goals, such a document can spell out expectations of performance and honesty. Second, all information about the works, resources, and participants needs to be spelled out. The Churia and RW programs in Nepal required this in the form of a project book containing descriptions of the works and activities, all relevant estimates and standards, work norms and wage rates, complete budgets, lists of committee members and laborers, and the minutes of project meetings. Mandatory keeping of public project books has made detailed resource information about projects accessible to any villager with someone in the family who could read it to him/her. The project books in this case provided a decisive governance tool, but only when users and consultants worked to ensure those responsible kept the books properly and provided public access.

Ensure regular public monitoring and discussion: The Churia and RW programs provided for a series of public events designed to disseminate information and air grievances. Where they occur regularly, public meetings to decide on project selection and design, public commitments of support and integrity by officials, public payments of rice and money, and public audits of works progress and wage payments have most project-related corruption much more difficult. The centerpiece of these communal events was the public audit, in which project staff read the project book aloud, made and discussed measurements, made and recorded wage payments, and discussed issues and problems. Supplementing and supporting this were regular (biweekly) inspection visits, and public delivery of rice in open carts. This public and observable conduct of business helped drastically reduce collusion and build active participation, and eventually trust, among beneficiaries.

Make the information usable and act on it: A transparent system, by definition, sends timely signals of project performance as well as the credibility of the transparency mechanisms themselves. Attendance at village audit meetings increases when programs are successful. Where attendance is too small e.g. less than 50 percent of users, meetings are not held, or if held, signal an erosion of confidence and possible corruption. The project book is also very important, and its use shows how effectively the project is performing. If it is completed and readily available to anyone, if villagers have seen it and discussed its contents, if everything is written in, then the project is going well. If it is incomplete, not available, or does not reflect known problems, then something is likely to be wrong. Especially in those areas where the Churia approach has proven successful, greater transparency has also improved trust,

started to erase bad feelings between the civil service and local people, and helped create a more positive view of government among ordinary people.

However, there is also the potential for popular frustration when the response does not live up to expectations. The increasingly frequent news reports of corruption have triggered a few investigations but have done little in practice to curb endemic corruption in Nepal. Likewise, dissemination of project information does not accomplish much where the information is incomplete (or inaccurate) and where potential users of the information, such as program beneficiary communities, are incapable of acting on it. Signboards can conceal information as well as publicize it, and the wage figures in public project books are of little help if workers cannot read them, or if there are no other constraints on the ability of project overseers to levy informal taxes. Public audit systems can also have drawbacks, including the absence of procedural safeguards and inaction by officials who are fearful of the audits.[88] In short, information flows are most effective when coupled with appropriate incentives and accountability mechanisms – and when these lead to action.

3. *Align incentives (as an urgent priority).*

"Incentive structures" are a staple of the anti-corruption literature. As with the other matters discussed here, it is important to consider what this means in the dysfunctional environments of most poor countries – i.e. where incentives are generally perverse. In these situations, it essentially means insulating programs to the extent feasible from prevailing systems of public sector corruption, and setting up appropriate incentives in areas under the program's control. These strategies tend to overlap or converge – for example, one means of insulating a program from existing corruption may be to offer countervailing incentives.

Cocoon if the situation requires it: There are two main approaches to cordoning-off programs to ensure integrity. First, some form of direct program implementation by the donor agency ("cocooning") should be considered if chronic and severe bureaucratic corruption warrant it. As in the Nepal example, this could mean delegation of project implementation to a third (non-governmental) party, which is accountable for expenditure and project implementation verification. The program design must minimize officials' discretionary control of program-related resources, since these are likely to be thoroughly exploited when any opportunity arises.. In situations of endemic corruption, this is likely to be crucial at least for an initial period (perhaps two years), while transparency standards and expectations are being established for the first time.

This approach requires a staff of reasonably paid and accountable professionals outside the civil service structure. Although such an approach can be criticized generally as subsidizing a program enclave, or as unsustainable, it can nevertheless be valuable as a means of maximizing program benefit/cost, shaping beneficiary expectations about governance, and establishing patterns of integrity that can be applied to the public sector. This approach was taken in the Churia program in Nepal, and appears to have had these beneficial effects. In that case, it was critical for Consult to exercise full control over rice and cash to be paid out, design and estimation approval, purchase of materials, and overall monitoring. In the circumstances, this radical approach appeared to be the only way to ensure that program resources were used productively, and that the cycle of theft and cynicism could be broken long enough to breed new expectations of governance.

Use ringfences and bureaucratic incentives with care: The second approach to protecting

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[88] Helvetas (1998).

program resources from systemic corruption is sometimes called "ringfencing." This frequently involves the establishment of project units within the government, sometimes with donor financing. The donor agency and the government may negotiate detailed rules and procedures to be followed in program implementation, as a condition of the external support. This approach has been used in the RW program, but with less success than the approach of full delegation to an outside entity. To the extent the program is functioning well, this appears to be mostly a result of effective work by the consultants and community mobilization.   The ringfencing approach appears to require both a modicum of civil service professionalism as well as a serious commitment by the host government and donor agency – conditions that did not obtain in Nepal. As a result, the move from a cocoon model under Churia to a ringfence model under RW was only partially successful.

To the extent that some counterpart resources were within government control under Churia, that program had to grapple with ringfencing and incentive issues as well. Bureaucrats in a dysfunctional system will exploit whatever aspect of a program is under their control. Two methods are available to combat this: reducing bureaucratic control of relevant resources as far as possible, and providing appropriate incentives for bureaucrats with program support. The Churia program located control of all important program resources with the consultants and communities, leaving government a role to play in some aspects of logistics, largely with its own resources. By contrast, RW acknowledged government as a full partner, placing it principally in charge of rice storage and transport, and bringing program implementation within the ambit governmental planning systems, and policies on work norms and rates. This approach put a much larger share of program-related resources at risk of misappropriation.

This difference also means that the Churia and RW programs place differing levels of importance on bureaucratic incentives. In carrying out a program within a dysfunctional environment such as Nepal's, some consideration must be given to providing pay incentives (e.g. performance-based top-up payments) to officials involved in the program activities, since pay shortfalls appear to be a major inducement to corruption. Here, there is a tradeoff between near-term reduction in program-related corruption and longer-term distortion of civil service effort (i.e. concentrating effort where top-ups and allowances are available, and exerting pressure for more of such payoffs). Experiments with these incentives in Nepal were largely unsuccessful, due to the unreliability of pay supplements and their small size as compared to potential illicit earnings.

Design and reinforce community incentives to combat corruption: The focus of the discussion thus far has been on *bureaucratic* incentives. Given the role that beneficiary *communities* can play in rural infrastructure programs, how can their incentives be optimized? In the Churia program, when they recognized that any theft of project resources would reduce benefits accruing to them, villagers became much more willing to fight corruption. The requirement of a partial local contribution to projects reinforced community incentives for effective monitoring, essentially by putting a sunk investment at risk.

How can one reinforce local motivation to combat corruption when voice and accountability have been absent in the past? One way is for program consultants to provide external verification and validation of key community decisions. Villagers usually fail in their efforts to control corruption because they have no leverage over civil servants or local elites. In Nepal, the Churia program consultants provided communities an integrity "anchor." Using project consultants as their development partners, local villagers fought successfully against problems such as arbitrary decisions about projects, payoffs to overseers and engineers, rice theft or delivery of unacceptable quality rice, improper earthworks

measurements, and employment favoritism.[89]   A major flaw of the RW program was that it greatly diminished the external consultants' power to resist traditional corruption or to stop implementation if they found situations that the villagers knew were wrong.   Politicians also valued the independent consultants, since they felt that the latter provided a safe place to ask questions and to help change the political balance with the civil servants. (Here was one of several instances where politicians' interests were aligned with their constituents'.)

Another means of reinforcing community incentives to restrain corruption is to expect integrity and to reward it. From the start, a firm standard that corruption and cheating are unacceptable should be established and consistently applied by all parties. This, of course, implies the need for "sticks" -- agreed sanctions for corruption and cheating were established, but at the same time, people were allowed to atone and repay. Also, the program made the funding of projects conditional on the use of local norms and counterpart contribution, and the release of rice and cash required complete observance of the rules (public audit, etc.). At least as important are the "carrots" – where feasible, integrity should be rewarded. For example, the Churia program team informed villagers that if they completed their projects rapidly, responsibly, and honestly, they would be eligible for other projects in the future. Where time permitted, follow-on projects were awarded to deserving VDCs. Villagers communicated to each other frequently, and the word got out that integrity was rewarded. This reinforced efficient project operations, and created an environment where it became very costly to cheat.

4. *Donors should act responsibly as governance institutions (because they are).*

The role of donor agencies in reinforcing good governance is difficult to overestimate. At a minimum, given the fungibility of aid resources, they underwrite much of what client governments do, for good or ill. They can also drive recipient government policy priorities. This is especially so in the case of aid-dependent countries such as Nepal. Donors must shoulder this responsibility squarely, realizing that any neglect or cynicism on their part can contribute directly to local waste and corruption.

Send clear signals that integrity is important: As the Churia experience demonstrates, the illicit tax of corruption can be avoided or reduced through serious attention to program-related institutional design and follow-through. This is as much a donor responsibility as a governmental one, and in practice the choice is frequently between donor action or none at all. Thus, donor agencies' decisions about whether to insist on clear standards, accountability, and transparency can play a leading role in determining the extent of program-related corruption. Thus, a strong donor commitment to effective program governance sends signals – of support for those struggling to strengthen governance, of warning to those intending to engage in abuses – that can bring tangible benefits in terms of program governance. A wavering or reluctant engagement in this area suggests to counterparts that abuses will not be taken seriously.

Avoid reaching other goals at the price of tolerating corruption: Traditionally, internal donor agency incentive systems have placed highest priority on timely performance of project tasks and, in particular, the use of budgeted funds.   In addition, the arrangements are usually directly with the government, regardless of the latter's capacity to complete the tasks envisioned.[90]   Where government systems create opportunities for corruption, donors in the past have usually either looked the other way or

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[89] Accountability in some cases has outstripped available safeguards. In at least two cases, persons who stole project rice were beaten by villagers until they returned the rice.
[90] As is well known, donors are moving increasingly to implementation via international NGOs and local NGOs, in response to the very poor project performance in the past under government implementation.

attempted to make changes at the margins rather than pushing for reform. Even apart from internal reward systems, the larger diplomatic, political, and economic objectives of an aid provider may seem to require hard-nosed realism – i.e. misappropriation of some donor and counterpart resources may be a price worth paying.

The messy reality of development makes it difficult to eliminate such trade-offs entirely, but their costs should be kept clearly in mind, and steps taken to avoid them whenever possible. Tolerance of corrupt practices as the price of on-time project completion can only abet local efforts to increase the margins for corruption. Such acceptance can drastically reduce the benefits to rural communities and distort incentives further in favor of redistributive rather than productive activity on the part of officials and private agents. Can we say with confidence when this approach is appropriate? Donors in Nepal have argued that "certain levels of losses are acceptable, especially in comparison to previous systems."[91] Is this true, even in its own terms? This appears improbable, especially since the alternatives include not only a tougher line on integrity in program implementation, but also the option to "just say no." In Nepal and many other countries, some hard thinking is required about whether a program is appropriate at all, in light of systemic corruption and other problems, and if the program moves forward, how it might both be shielded from the worst effects of corruption and contribute to systemic reform.

Build carefully on success: Where programs such as Churia succeed, not only must the lessons be understood, but the donors should commit themselves and their counterparts to a replication that remains fully consistent with the key determinants of the previous success. By contrast, in designing the follow-on RW program in Nepal, the donor agencies appear to have paid insufficient attention to the main components of the original model. Some of the changes introduced in RW are said to have been justified by the need for full partnership by the government. However, implementation through the same system encouraging corrupt practices in the past is unlikely to slow corruption. A complete return to business-as-usual would mean that, while a program might achieve immediate goals of expending a quantum of project resources in return for a given level of civil works output, up to one-half of all project resources may be diverted to personal – or political -- use. Success can easily be turned into failure.

5. *Break out of the cocoon whenever possible.*

Observance of sound governance principles, such as those embodied by the Churia model, should not stop with the establishment of an individual program as an enclave of probity (if at all possible). Public works projects fit within an evolving scheme of governance encompassing local, national, and intermediate levels, and these projects can provide test cases for the elaboration and implementation of governance reforms. Successful cocooning may increase the local sense of entitlement to autonomy, control, integrity, and transparency. This can have important spin-off effects.

Enable communities to apply transparency mechanisms more broadly: Although cocooning cannot be a long-term solution to governance failure, its successful application can foster sustainable improvements. In the case of Churia in Nepal, the free-standing implementation structure financed by the donor worked closely with and affected other structures, especially User Committees but also bureaucracies. The key elements of governance in this model were mutually-supportive: local voice and ownership, the use of negotiated local work norms, open channels for the flow of project information, transparency and public audit, management of projects by representative local committees, civil servant incentives as appropriate, and reliable external support and monitoring. Thus, the project enabled

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[91] Direct communication from senior donor representative, October 1997.

communities to co-produce necessary infrastructure while monitoring the use of resources and holding bureaucrats to standards of integrity.

This dynamic can, and in some instances in Nepal did, continue beyond the completion of the infrastructure projects. In several instances, a variety of funding sources have been used by villages for follow-on projects using this governance mechanism, even where the donor-funded programs are not operating and have not been active for some time. Here, communities both obtained immediate benefits and recognized that they would continue to gain if they carried on using similar methods. Some of the benefits of accountability are both tangible and automatic, e.g. improved project benefit/cost and the longer-term value of built infrastructure. There may also be benefits from more democratic processes, as well as specific political gains. In the case of Churia in Nepal, villagers at the local level were impressed with the notion of transparency as a political obligation of democratic systems. They discovered that they had power to influence local activities, and pressured both User Committees and district-level staff to perform their functions rapidly, properly, and without taking bribes. Such change may be rapid and dramatic at first, but it must be remembered that lasting attitudinal change of this kind is usually slow.

Emphasize the benefits to political allies: Few things guarantee sustained momentum for reform more effectively than demonstrable political benefits. Although this has been subject to some debate, the Churia project districts did score some political gains from their participation in the program. While some politicians felt that they lost their elected seats due to pushes for integrity, others who were elected or re-elected were convinced that their commitment to local norms and public audits made them more popular. Even some of those who lost felt that the demonstration of integrity would benefit them politically in the long run. At the VDC level there was a clear link between those who had been active on User Committees in VDCs with completed works, and their subsequent first-time election as VDC representatives or chairmen. Some district and village politicians concluded that the public audit and local norms systems could be modified and applied to fiscal transfers and other issues at the village and district levels.

Encourage policymakers to adopt the transparency mechanisms formally: The best evidence that any governance model has broken out of its enclave to influence the system at large would be its formal adoption by government. The Churia and RW programs did indeed have some influence of this kind, though the policy response has been modest. In some areas, the VDC and DDC staff have carried on with government-funded projects using the Churia governance mechanisms, and in many of these villages, local contributions have been pooled for self-managed projects such as temples or ponds. Locally-determined work norms are now required in principle for project funding under the government's VDC Self-Reliance grant program (although questions have been raised about the extent to which this rule is followed in practice). After the Churia program's precedents were examined by other donors in Nepal, mechanisms such as public audits are now being required in some large programs funded by the World Bank and the Netherlands, among others.

On the whole, however, the Churia and RW programs have not yet led to major systemic reforms. This is a weakness of programs focusing on rural livelihoods and infrastructure: the best they can usually hope for is to ensure efficient project implementation, to protect donor-provided resources, and to exercise a modicum of influence on relevant officials. Those involved in the programs would acknowledge that the performance of rural works projects occurs within both a narrow project design and a wider framework of governance. Thus, the systems of budgeting, expenditure control, public procurement, civil service pay and discipline, and intergovernmental fiscal relations play a critical role in determining applicable controls and incentive structures. In light of this, an alternative design might incorporate a formal institutional reform component addressing those systemic issues directly with

government, in tandem with project-specific influences. To our knowledge, this has not been tried. The obstacles to such an approach are surely daunting, but the potential gains are also large.

6. Develop strategies to confront resistance (because it's inevitable).

Of course, attempts to strengthen the above elements of governance will face resistance from groups who stand to lose. These include politicians desiring patronage rewards to dispense, civil servants seeking to increase their remuneration illicitly, and the brokers and rent-seekers stationed at control points between the national and local levels. When a project or a reform endangers the benefits of corruption to these stakeholders, they can be expected to fight hard to ensure its failure, and to claw back any benefits they've lost at the first opportunity. Experience in Nepal suggests a few approaches to countering this.

Forge alliances to outflank the corrupt: The present case suggests that both local political bodies and central agencies contain potential allies. Newly-elected local politicians frequently make graft-fighting part of their electoral platform. Regardless of how dedicated they remain to this goal after becoming accustomed to holding office, such representatives have responded to local calls for integrity-enhancing change, such as the use of local work norms and transparency in the use of central grant funds. More experienced politicians can also sometimes be counted on, especially if they have been relatively insulated from the corrupting influence of national "money politics." Central ministries at times have agendas and approaches that are compatible with local efforts to improve governance, for example the policy of using local work norms adopted by Nepal's Ministry of Forestry at the time of the Churia program. In these instances, ministries may serve as supports for integrity, against the efforts of other agencies and bureaucrats to safeguard systems of illicit extraction. The same alliances can provide vital help when threatened interests become obstructive, or level false accusations at program staff.

Tie officials' hands in public: This tactic is now broadly recognized in the "integrity pledge," which provides the foundation for an "island of integrity." Here, all relevant stakeholders are asked, cajoled, perhaps pressured in public forums to take a stand against corruption -- in effect, to pledge support for integrity and to undertake its defense within the protected sphere (e.g. international tenders). In Nepal, a more modest form of this was used by the Churia program consultants to rope local politicians and bureaucrats into supporting the goal of a clean and efficient program. Any back-tracking on this commitment, any contradictions, any inconsistent behavior thus became a potential source of public comment and public embarrassment. Of course, by itself, this cannot control secret behavior, but it can send a strong warning signal and encourage other stakeholders to act as monitors. Sometimes, this has been enough to induce politicians and officials to regard a given program as "off-limits."

Set an uncompromising example: Exerting public pressure to constrain corruption usually entails the demand that those in power conform their behavior to integrity standards. It is unlikely for such a demand to be taken seriously, by those to whom it is directed or by others who may need to act as monitors, if the behavior of those making the demand does not strictly accord with the standards being advocated. Moreover, donor agency personnel and implementation consultants (or NGOs) – especially in a "cocoon" model – take on some of the roles of public servants. They therefore need to lead by example. Zero tolerance of infractions, abstemious standards of behavior, and limits on social exchange that may sometimes be regarded as hostile (e.g. refraining from sharing food, drink, or small exchanges) may all be required to break an existing "culture" of corruption. The Churia team in Nepal used these methods effectively to set a tone of high integrity in the program. Where this example attracts a wide following in the community, it also provides social incentives for people to enforce it and increases the pressure of expectation on officials to follow suit.

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